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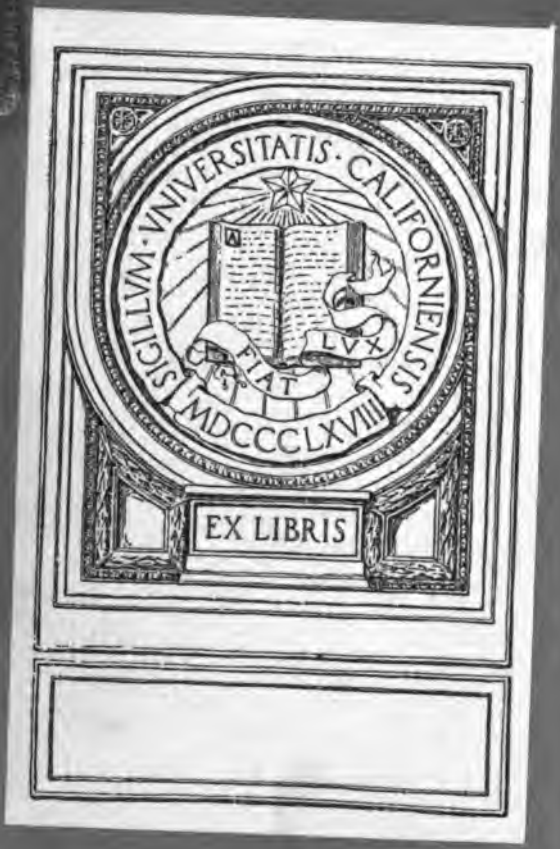
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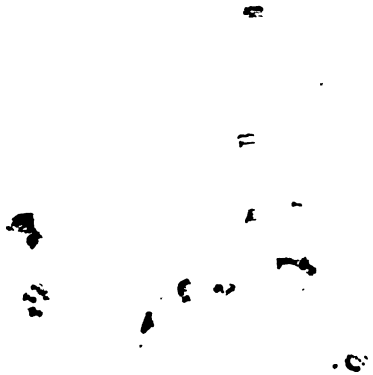

THE TRUST PROBLEM

IN THE

UNITED STATES

BY

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New York

THE MACMILLAN COMPANY

1921

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Set up and electrotyped. Published December, 1921

464008

Printed in the United States of America

TO MY WIFE

PREFACE

This book is a study of the trust problem in the United States. It presents an account of the early devices employed to restrain competition, and outlines the history and character of the modern trust movement; it describes a number of representative trusts; it analyzes the reasons for the formation of trusts, and their economic and social consequences; it describes the trust legislation, the decisions of the courts interpreting it, and the dissolution proceedings brought under it; and, finally, it considers (briefly) remedies.

The book is not a study of all combinations, but merely of those combinations that have (or had) monopolistic power, and that are properly designated as trusts. It is a study of monopolistic aggregations of capital under unified management. It contains no discussion of the experience of foreign countries, and only a brief (incidental) discussion of the experience of our forty-eight states. Material on these subjects was collected, but is omitted from the book for want of space, and because of a conviction that the trust problem is a national one, to be settled in the light of the conditions of our particular national life. The analysis of the six representative trusts is not intended to be complete; the aim has been merely to present the data in sufficient fullness to bring out concretely the reasons for forming trusts, the sources of their monopoly power, their tactics, and their economic consequences. In general, the history of individual trusts is not carried beyond the date of the dissolution proceedings instituted by the Department of Justice of the United States. Adequate reliable data for the subsequent history of these trusts are not available; and, moreover, the purpose is not to present a complete history of the representative trusts, but to explain the national policy toward trusts as evidenced by our laws and the manner of their enforcement.

The outstanding feature of the trust problem is its complexity. In the preface to an earlier book—"The Anthracite Coal Combination in the United States"—the author, after a detailed study of the facts connected with a particular combination, took occasion to emphasize the complex character of the trust question; and time has only served to deepen this early conviction. There is, so it would appear, no one solution of the problem; for we are confronted by a complex group of issues that must be dealt with collectively if any solution is to be had. The method of approach to this complicated problem has been that of the scientific investigator. The author would be neither advocate nor accuser. We are, in truth, in the grip of mighty forces,—forces that are modifying fundamentally the world's organization of industry; and he would be rash indeed who would venture to predict with assurance what the immediate future holds in store for us—whether regulated competition, regulated monopoly, or public ownership in one form or another. Or possibly even some new untried venture into hitherto unexplored economic fields. The author is therefore content to present primarily a record rather than an argument—or a prophecy.

Grateful acknowledgments are due to my brothers Grinnell and Percival, and to Messrs. J. S. Davis, F. B. Garver, C. A. Huston, H. L. Lutz, William Notz, C. O. Ruggles, F. W. Taussig, A. C. Whitaker, and M. S. Wildman, all of whom read portions of the manuscript. But my deepest obligation is to my father, Professor Richard Jones, who despite the demands of his own rigorous intellectual life has given unstintedly of time and counsel, to the end that I should, with Shakespeare, try to 'find where truth is hid,' and then take heed lest I 'deliver' more or less than truth.

E. J.

Stanford University
November, 1920.

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CALIFORNIA

THE TRUST PROBLEM IN THE UNITED STATES

CALIFORNIA

THE TRUST PROBLEM IN THE UNITED STATES

CHAPTER I

INTRODUCTORY

The term "trust" in everyday speech is quite loosely used, and it consequently conveys a different idea to different people. It is thus essential at the outset to indicate clearly the sense in which the word is used in this book.

The trust, as the term is here employed, means industrial monopoly. It does not include monopolies (whether railroad or other) in the so-called public service industries. Nor does it include pools, trade associations, and other organizations which, though they may temporarily possess some power over prices, do not interfere with the substantial independence of the concerns involved. Yet neither is the term limited to the earlier and narrower concept of monopoly as an exclusive legislative or executive grant. A trust (industrial monopoly) may be said to exist when a person, corporation, or combination owns or controls enough of the plants producing a certain article to be able for all practical purposes to fix its price. Control over the price is the fundamental test of monopoly; it is its essential and characteristic feature. Just what percentage of the business must be handled by a trust in order that it may be able to determine the price of a given article can not be stated with precision, yet it seems fairly certain that as a general rule the production of from 70 to 80 per cent of the national supply, and possibly even less, is quite ample for price control. As was said by Mr. H. O. Havemeyer, long the head of the sugar trust: "It goes without saying that a man who produces 80 per cent. of an article can control the price by not producing; the price must advance if he

does not produce; and it must decline if he does produce, if he produces more than the market will take."[1] The term trust or industrial monopoly, therefore, is not identical with complete monopoly;[2] for without an exclusive grant of privileges a complete monopoly is not likely to exist, unless it be based upon the sole possession of a limited natural resource.

The concept of industrial monopoly here defined has been clearly described by the Supreme Court of the United States. In National Cotton Oil *v.* Texas, the Court said: "The idea of monopoly is not now confined to a grant of privileges. It is understood to include a 'condition produced by the acts of mere individuals'. Its dominant thought now is, to quote another, 'the notion of exclusiveness or unity'; in other words, the suppression of competition by the unification of interest or management, or it may be through agreement and concert of action.[3] And the purpose is so definitely the control of prices that monopoly has been defined to be 'unified tactics with regard to prices.' It is the power to control prices which makes the inducement of combinations and their profit."[4]

Just what is meant in this book by a trust may be made clearer perhaps by differentiating it from other forms of industrial organization. While there are many types of manufacturing organization, for the purpose of clarifying the idea of the trust we need distinguish but four: first, small-scale production; second, large-scale production; third, production by a group of plants united in a combination; and, fourth, production by a trust.

In the manufacture of many commodities, as is well known, small-scale operations still prevail. The following industries

[1] Lexow Report (New York), 1897, p. 111.

[2] In Patterson *v.* United States, 222 Fed. Rep. 619, the Circuit Court said: "To monopolize trade or commerce, or a part thereof, is to exclude persons therefrom. It is not, however, to exclude all persons." Were all persons to be excluded, the result would be a perfect monopoly, which in experience has arisen only from a sovereign grant (p. 619).

[3] The suppression of competition through agreement merely does not come within the author's definition of a trust.

[4] 197 U. S. 129.

will serve as examples: cigar, beet sugar, brick, gunpowder, bread, butter, cheese, ice cream, and fruit and vegetable canning. In the manufacture of a large number of other commodities, the size of the plant unit has greatly increased. As examples may be cited the following: oil, iron and steel, hard coal, soft coal, cane sugar, cigarettes, shoes, textiles, automobiles, harvesters, cash registers, shoe machinery, and meat. Experience has clearly proven that the articles mentioned, as well as many others, can be produced more economically in large factories than in small ones. It should be borne in mind, however, that what is considered a large factory in one industry would be a small unit in another industry. A $6,000,000 cotton mill, for example, would be regarded as a large plant, whereas a $6,000,000 steel mill would be a small-scale operation.

The combination frequently represents a third stage. A number of factories, each of which may have already increased the size of its plant to the most economical unit from the standpoint of production, may combine in order to secure the economies of large-scale management, in addition to the economies of large-scale production. This combination may be of two sorts. It may be a combination horizontally (so to speak) or a combination vertically. A horizontal combination is one that brings together under a single management several plants producing the same article, as, for example, a combination of fertilizer plants. A vertical combination is one that brings together a number of plants, each of which concerns itself with a separate stage in the production of the finished product. This is what is known as the integration of industry. As an illustration, a combination of a coal mine, an iron ore mine, a blast furnace, a steel mill, and a steel rail mill, is a vertical combination. Such a combination has its advantages, as it assures the manufacturer of steel rails an ample supply of raw materials at a reasonable price. The combination horizontally also has its advantages, as, for example, a saving in freight rates. A company with one plant at New York and another at Chicago can supply the intervening market from that plant which is nearest the point of consumption. Because of the obvious advantages of combination in certain lines of in-

dustry (of which more later), this form of organization has frequently been employed. The American Agricultural Chemical Company is an illustration of a horizontal combination; the Bethlehem Steel Company an illustration of a vertical combination. Some combinations, both horizontal and vertical, are formed without any thought of interfering substantially with the operation of competitive forces; others are resorted to expressly for that purpose. Yet even when the restriction of competition is the object of a combination, such is not always the result. The early iron and steel combinations, for example, merely intensified a competition that was already quite active.

The fourth form of organization is the trust, by which is meant a combination of a sufficient number of plants to secure practical control over the supply, and thus over the price.[1] Well-known trusts are the Standard Oil Company,[2] the American Tobacco Company,[2] the United States Steel Corporation, the American Sugar Refining Company, the International Harvester Company, and the United Shoe Machinery Company. Though trusts may by definition originate through internal expansion, in fact they have come into being almost entirely through an act of combination. They are thus horizontal combinations, yet of so far-reaching a character that they secure dominion over the industry. Trusts, morever, may be vertical combinations. Thus, the United States Steel Corporation is highly integrated, as are also the International Harvester Company, the Standard Oil Company, and the American Tobacco Company. Not all combinations, whether horizontal or vertical, are trusts, however; it is possible to effect combinations, both horizontal and vertical, that have no semblance of monopoly power.

[1] Mr. Kales, adopting the phraseology of the Department of Justice in the International Harvester Company case (Brief for the United States in United States *v.* International Harvester Company, no. 56, pp. 34–101), says that a combination to be a trust must embrace units which together occupy a "preponderant" position in a given industry. Harvard Law Review, 30, p. 830.

[2] The situation prior to the dissolution decrees of 1911 is here in mind. Whether the oil and tobacco trusts were effectively dissolved or not is considered in ch. 18.

The question at issue, upon which it is hoped this book will throw light, is: what public policy should be adopted toward trusts? Do trusts represent mainly an attempt to secure monopoly profits by raising prices, and should they therefore be prohibited and the endeavor be made to restore competitive conditions so far as possible? Or do trusts represent a more efficient business organization, and should they therefore be permitted to exist subject to governmental regulation of their prices and the like? Or, finally, is it difficult, if not impossible, to restore competitive conditions or to regulate satisfactorily the prices of trust-controlled products, and should therefore the monopolized industries be socialized? It is not assumed that this book solves these crucial problems, yet it is hoped that this presentation of the facts may contribute toward their solution.

CHAPTER II

POOLS

Whether or no such was the main reason for their formation, the trusts have in fact restrained or eliminated competition in their field. Yet some time prior to the modern trust movement attempts had been made through other agencies to restrain the free play of competition. Some familiarity with these other attempts is essential to an understanding of the trust movement.

The pool was the first and the commonest mode of restricting competition between manufacturers. A pool was formed in the brass industry as early as 1853;[1] and one in the cordage industry in 1861.[2] Yet until after the Civil War combinations among manufacturers were few in number and narrow in scope. The inadequacy of transportation facilities, and the comparatively small capital investment per firm, prevented manufacturers from reaching out to any considerable extent into the territory of their potential rivals; and there was thus less occasion for association. But with the rapid growth of business after the Civil War and the development of large-scale production, keen competition appeared. To check this competition pools were formed; and they have been numerous ever since. At the present time they are probably more numerous and varied than ever before. Even some of the leading trusts, such as the United States Steel Corporation, have had pooling agreements with the independent producers; and some pools are international in scope.

The term pool as here used is a catch-all for the various agreements and associations whereby a number of concerns, each preserving its own organization and to a large degree its own independence, adopted provisions looking toward the main-

[1] Lathrop, The Brass Industry, p. 121.

[2] Dewing, Corporate Promotions and Reorganizations, p. 114.

tenance or raising of the prices of the articles produced by them —the power actually to fix prices may or may not have been conferred on a governing body—or looking toward the depression of the prices of the materials and supplies required by them. The pool in the industrial world may be compared, so far as its organization is concerned, to a League of Nations in the political world. The members of the pool, like the members of the League, retain full control over certain matters, but temporarily delegate certain powers to a central organization. Upon the disbanding of the pool, as upon the dissolution of the League, the members resume complete control over their affairs.

Pools are of numerous kinds, but six leading types[1] may be distinguished: first, the gentlemen's agreement; second, the speculative pool; third, the regulation of the output pool; fourth, the division of the field pool; fifth, the selling agency; and, sixth, the patent pool.

First. The gentlemen's agreement is perhaps the loosest form of a pool.[2] As its name implies it is simply an agreement between gentlemen looking toward the control of prices. As the agreement is between gentlemen, no formal organization is created, and no contracts or papers are signed. Under the gentlemen's agreement there is no provision for the payment of penalties in the event of a violation of the agreement; such is not assumed to be necessary, since the members are expected to abide faithfully by their informal promises. Gentlemen's agreements have been very numerous in the iron and steel industry; in fact at some time or other they have been found in every branch of the industry.[3] They were employed also on several occasions in the

[1] No claim of comprehensiveness or all-inclusiveness is made for this classification. It does not include, for example, those wholesalers' or retailers' associations which Mr. Stevens calls legitimate trader associations. See American Economic Review, 3, p. 555.

[2] Some authors, for example, Mr. Haney (Business Organization and Combination, 1915, p. 146), do not classify a gentlemen's agreement as a pool. This is because they give to the term pool a narrower and more restricted meaning than is employed in this text.

[3] Report of the Commissioner of Corporations on the Steel Industry, part I, p. 75.

anthracite industry.[1] However, mere agreements rarely proved successful, since there was nearly always at least one "black sheep" whose infractions of the agreement led to its abandonment.

Second. The speculative pool, being organized for speculative purposes, is a temporary arrangement, which is ordinarily terminated as soon as the object of the pool has been attained. Perhaps the best illustration of this type of pool is the French Copper Syndicate, organized in October, 1887. This syndicate entered into contracts with the producers of copper in other countries for the purchase, at a figure somewhat above the market price, of all the copper produced by them. The syndicate hoped to corner the world's supply of copper, and at the time the contracts were entered into did control from 80 to 85 per cent of the total supply. The financing of these purchases was, of course, a difficult matter, particularly since the output of copper greatly increased under the stimulus of abnormally high prices. Unfortunately for the syndicate there occurred a run on the bank which was providing the funds, and as a result the syndicate speedily collapsed. Subsequently the price of copper fell much below what it had been prior to the formation of the pool.[2] Because of the fact that speculative pools were temporary in nature and difficult to finance, they were not satisfactory to the manufacturers seeking some device whereby they might effectively throttle competition.

Third. A common type of pool is one which endeavors to regulate the output, and thus indirectly to regulate prices. Such a pool may take various forms. Power may be given to a central committee to order a curtailment of the output of the individual mills, as in the cotton bagging pool of 1888.[3] More commonly, however, the members of the pool through a process of discussion agree upon the total output and upon the division of this output among themselves in certain definite proportions. This was the form of agreement for many years in the anthracite coal industry,

[1] See Jones, The Anthracite Coal Combination in the United States, ch. 3.

[2] Andrews, Quarterly Journal of Economics, 3, pp. 508–516.

[3] House Report no. 4165, 50th Cong., 2nd Sess., p. 144.

although the agreement here was between the railroad companies, rather than between the coal mining companies. Each railroad (all of them were engaged in the mining of coal either directly or indirectly) was allotted a certain percentage of the total shipments of anthracite coal, and was expected to take care that the amount of coal shipped by it, including that carried for independent coal mining concerns, did not exceed this percentage. Sometimes penalties were imposed for the violation of these agreements; at other times not. When provision was made for penalties, the railroads exceeding their allotment contributed to a fund, which was distributed among the railroads that had carried less than their allotment.[1]

One of the most important pools regulating output was the steel rail pool, formed in August, 1887.[2] The members of this pool produced more than 90 per cent of the country's output of steel rails. By the agreement adopted the total output as then agreed upon was divided among the companies in definite proportions, and provision was made for a Board of Control, which, with the written consent of 75 per cent of the tonnage, might increase the pool's output from time to time. The fixing of prices was not provided for in the memorandum of agreement, though an informal understanding was reached. This pool was comparatively successful. The large capital necessary for the manufacture of steel rails discouraged new competition, and the practice on the part of railway officials of buying the necessary rails once a year acted as a stabilizing factor. Nevertheless, the pool collapsed in 1893, because of a disagreement over the division of tonnage, the situation being aggravated by the prevailing industrial depression, which rendered imperative a reduction in the total output. In 1894 the pool was reorganized, though not without considerable difficulty. The depressed state of the trade led to new violations of the agreement in 1896, and in February of the following year the pool was again broken up.

[1] Jones, The Anthracite Coal Combination in the United States, pp. 41–50, 54–56.

[2] Report of the Commissioner of Corporations on the Steel Industry, part I, pp. 68–72.

This second dissolution of the pool was followed by a drastic reduction in prices. Whereas the pool price for steel rails had been $28 per ton, upon the termination of the pooling agreement the price fell to $16.50.[1]

Another important pool in the steel industry was the so-called wire nail pool, organized in 1895.[2] The Association of Wire and Cut Nail Manufacturers provided for a division of the output among the members of the association, and also fixed the amount of nails to be offered for sale each month, and the price at which they should be sold. Immediately upon its organization the pool advanced the price of nails. Whereas the "base" price had been $1.20 per keg in June, 1895, by May, 1896, it had risen to $2.55. In view of the fact that no large amount of capital was required to engage in the nail business, it was to be anticipated that the life of the pool would be short. Whether or no its existence was prolonged by its audacious price policy, it came to an end in December, 1896, about a year and a half after its organization.

A pool in the meat-packing industry was organized as early as 1885; and since that date pools of one kind or another have been maintained almost steadily.[3] The pool of 1885 determined the quantity of meat that each member might ship, and by this means succeeded in exercising considerable control over the price of meat. In 1893 a more complete and effective agreement was entered into. As the result of this agreement the representatives of Swift and Company, Armour and Company, and Morris and Company held weekly meetings, which were occasionally participated in by representatives of the Cudahy Packing Company, and Hammond and Company. At these meetings each of the companies reported on its shipments into designated territories during the previous week and on the prices received. These reports served as the basis for the payment of fines for

[1] Brief for the United States in United States *v.* United States Steel Corporation (no. 481), vol. I, pp. 167–168.

[2] Report of the Commissioner of Corporations on the Steel Industry, part I, pp. 72–73; and Edgerton, Political Science Quarterly, 12, pp. 246–272.

[3] Report of the Federal Trade Commission on the Meat-Packing Industry, part II, ch. 1.

overshipments (40c. per 100 lbs.), and for the allotment for the ensuing week. In order that full secrecy as to these arrangements might be maintained and the consequences of legal proceedings avoided, the parties to this agreement were designated by certain letters of the alphabet rather than by their real names. This pooling arrangement continued from 1893 to 1896. During 1897 the pool was not effective because of the competition of Schwarzschild and Sulzberger, an important company not a member of the pool. The following year a new pool was entered into, including this time the firm of Schwarzschild and Sulzberger. This arrangment lasted until April, 1902, when because of the public agitation against the packers a decision was made to dissolve the pool. Thereupon the secretary destroyed all the records of the meetings of the pool.

The chief difficulty in this third type of pool lay in securing an agreement upon the percentage allotment, both at the organization of the pool and upon its renewal from time to time. An agreement might be reached at the time the pool was organized for an allotment based on capacity, previous sales, or what not. Yet this did not remove the difficulty; for each company was strongly tempted to enlarge its plant, in order that upon the expiration of the pool it might demand an increased percentage as a condition of entry into a new pool. If this demand was not acceded to, as it commonly was not, it became impossible to effect a renewal of the agreement; and with the increased facilities for production the market was flooded, and prices fell, perhaps even lower than prior to the formation of the pool. This was well illustrated in the experience of the steel industry. Upon the disruption of the steel rail pool in February, 1897, the price of steel rails fell to $16.50, which was about $4 per ton below the average price of rails during the six months preceding the organization of the pool.

In these pools regulating or apportioning the output there may or may not have been an agreement as to price. In the anthracite railroad pool of 1873, for example, a schedule of prices was agreed upon, and authority was given to a Board of Control to determine the prices to be charged from time to time; while in

the pool of 1885 in this same industry nothing was said in regard to prices. The steel rail pool of 1887 was silent on the subject of prices; but the powder pool of 1889, known as the Fundamental Agreement, gave a central board full power to fix prices. Yet whether or no any price-making machinery was set up, it was regulation of prices that was in the minds of those [redacted] were instrumental in organizing output pools. Obviously [redacted]es could not be maintained, much less advanced, unless the separate concerns were prevented from increasing their output at will; and the regulation of the output was thus the means whereby the desired control over prices was to be exercised.

Fourth. A good illustration of a pool providing for a division of the field is the agreement between the Addyston Pipe and Steel Company and five other corporations, all engaged in the business of manufacturing cast iron pipe, and selling in particular to municipal corporations, gas companies, water companies, and large institutions accustomed to invite bids from various concerns.[1] Under this agreement, entered into in 1894 and modified in 1895, the companies divided the United States into three parts: reserve cities, free territory, and pay territory. The reserved cities were reserved for certain companies, and none of the other companies was to do any business there. Free territory was territory in which any one of the companies could make sales without restriction. But the bulk of the United States (thirty-six states in all) was designated as pay territory; and in this territory (in which the companies had a practical monopoly because of the limitations on competition imposed by high freight rates) the conditions of carrying on business were definitely laid down. The six companies were to refer all inquiries for pipe in this section to a representative board, and this board was to fix the price at which all pipe in pay territory should be sold. The companies were then to bid on the order, and the one that offered to pay the highest bonus obtained the contract, which was to be executed at the price already set by the board. In order that the existence of the pool might not be

[1] 175 U. S. 211–248; and Argument of Hon. E. B. Whitney, Ripley's Trusts, Pools and Corporations (1916), pp. 78–96.

suspected, the other companies were to make fictitious bids, bids sufficiently high to insure that the contract would not be awarded to them. At the end of each year, after deducting the expenses of the association, the bonuses were to be divided among the members of the pool on the basis of their annual shipments into pay territory. The profits of each company, therefore, consisted of the excess of the price over the cost on the jobs awarded to it, plus the bonuses received by it on work taken by the other companies. These profits were greater, of course, than they would have been without the agreement, since the price to be charged for pipe was fixed by the representative board, and therefore was not subject to competition between the companies. In 1899 this pool was declared illegal by the Supreme Court of the United States.[1]

A division of territory was also established by the wire nail pool; and more recently by the meat packers as regards their purchases of cream and butter.

In the tobacco industry an international pool providing for a division of the field was effected. In September, 1902, the American Tobacco Company (the American trust) and the Imperial Tobacco Company (a British combination) entered into an agreement whereby the trade of the United States, Cuba, Porto Rico, Hawaii, and the Philippines, was reserved to the American Tobacco Company, and the trade of Great Britain to the Imperial Tobacco Company.[2] A new concern, the British-American Tobacco Company, owned by the two companies above, was organized to handle the export business in the rest of the world. The earth, like Cæsar's Gaul, was divided into three parts.

International pools have also been established in the steel rail, thread, glass bottle, aluminum, gunpowder, calcium carbide, and meat industries.

Fifth, Pools sometimes are merely selling agencies. The manufacturers turn over their total output to a central selling

[1] See p. 395.

[2] Report of the Commissioner of Corporations on the Tobacco Industry, part I, pp. 166–176.

bureau, which makes all the sales. A good illustration is the Michigan Salt Association, an organization of salt producers effected in 1876.[1] This association handled 85 per cent of the salt output of the important Michigan field. The producers made a contract with the association every year, and under the terms of the contract they agreed to deliver to the association all the salt produced by them during the course of the year. Each member reserved the right to produce as much salt as he pleased, yet since the association had complete charge of sales, it could adjust the price in such manner as to prevent overproduction. This association expired by limitation in 1881, but was immediately reorganized under another name. In 1886 it was again reorganized, this time under its original name. The salt association on the whole was quite successful. This success may be attributed to the fact that, like all selling agencies, it did away with price cutting by the members as a means of securing increased business.

A more recent illustration is the Continental Wall Paper Company (1898), a New York corporation, the stock of which was subscribed to by a group of concerns manufacturing 98 per cent of the country's output of wall paper.[2] As the selling agent for the companies in the pool, the Continental Wall Paper Company purchased the total output of these companies at prices fixed in the agreement, and distributed the profits among them in proportion to the capacity of their works. But the Continental Company was more than a mere selling agency. Its directors were constituted a committee with control over the production of the individual factories, and the prices at which wall paper should be sold to the trade. The company, it was agreed, was to compel jobbers to sign an agreement to buy only from members of the pool and to maintain prices. To add to the protective force of the tariff duties, an arrangement was made with the Canadian wall paper manufacturers, whereby each group agreed not to compete with the other. Finally, the only two manufacturers in this country of wall paper machinery were

[1] Jenks, Political Science Quarterly, 3, pp. 83–86.

[2] 212 U. S. 227–274.

induced to confine their sales of machinery to members of the pool.[1]

Of this arrangement the Circuit Court said: "A more complete monopoly in an article of universal use has probably never been brought about. It may be that the wit of man may yet devise a more complete scheme to accomplish the stifling of competition; but none of the shifts resorted to for suppressing freedom of commerce and securing undue prices, shown by the reported cases, is half so complete in its details."[2] Nevertheless within a very few years the Continental Company found its power gone. The increased prices initiated by the company led to the formation of new concerns, particularly since a market was immediately available through the Continental Company; and it proved impossible to control the jobbers.[3] The liquidation of the company was therefore determined upon, and this step occasioned no difficulty, since the company did not own any operating properties.

Sixth. A sixth type of pool is the patent pool. In 1896 the General Electric Company and the Westinghouse Company—controlling between them some 90 per cent of the manufacture of electrical supplies—entered into a pooling agreement for the joint use of substantially all their patents.[4] This agreement put an end to costly litigation, and also, it was reported, to competition for the acquisition of additional patents from inventors.

Some pools are founded on the ownership of patents essential to the manufacture of a particular article. Thus, certain manufacturers of enameled iron ware, owning valuable patents, joined forces and agreed to permit the use of these patents by manufacturers generally upon the payment of royalty and upon the execution of a license.[5] The license agreement established a schedule of prices, which the licensee (the manufacturer) agreed to

[1] 148 Fed. Rep. 947.
[2] *Ibid.*
[3] Industrial Commission, XIII, p. 284.
[4] See Chron., 62, pp. 476, 502 (1896).
[5] 226 U. S. 20–52.

observe; and provision was made for changes in prices from time to time by the licensor with the approval of a committee representing the manufacturers. Moreover, the jobbers were brought into the deal by the refusal of the manufacturers to sell to those jobbers who did not sign an agreement to handle only the goods of the licensed manufacturers and to maintain the resale prices as fixed from time to time. The government claimed that this was a price-fixing device in the guise of a licensing arrangement for the common use of patents and was sustained in this contention by the Supreme Court.

Having indicated the forms that pooling arrangements have taken, we may briefly point out the advantages and the disadvantages of pools as a device for restraining competition. With respect to the advantages, the pool provided a means whereby manufacturers could coöperate in regard to prices and trade conditions without entirely sacrificing their independence. The American business man was an individualist, and thus looked kindly on a business arrangement that increased his profits and yet left him largely the manager of his own affairs. The pooling system had the further advantage of not removing the financial inducement to economical administration of the individual properties. Since each manufacturer continued to operate his own factory, it was possible for him to increase his profits, not only through better prices, but also through such economies in production and selling[1] as he might individually put into effect. (However, the financial inducement—though it was not removed—must have been impaired, as compared with true competitive conditions, in view of the fact that a manufacturer who desired to increase the size of his plant in order to realize the economies of larger-scale production would certainly experience great difficulty in securing assent to an increase in his percentage allotment.) A third advantage was that the pool did not cause overcapitalization nor increased expenses in the way of taxes and fees. Finally, it provided a flexible form of organization, which could

[1] Except when, as in the central selling bureau, he no longer conducted the sales.

take on different forms by way of adjustment to the varying conditions in each industry.

Experience has shown that pooling agreements have more generally been attended with success when there were present the following favoring factors: (1) the requirement of large capital expenditure as a condition of economical production—this prevented competition from arising so readily; (2) as a corollary of the above, a small number of concerns involved—this facilitated the establishment and maintenance of a compact organization; (3) a willingness to adopt a farsighted policy with respect to output and prices—high prices might temporarily increase profits, but they stimulated competition, and thus eventually led to increased output and lower prices; and (4) a certain degree of uniformity among the members of the pool with respect to the size and nature of their business—this tended to give each member a common interest in the success of the pool.

On the other hand pools have proven to be weak in at least two important particulars. (1) They have not been able to maintain a sufficient degree of stability with respect either to prices or to industrial policy. The individual members of the pools still retained a large degree of autonomy, and their conflicting interests frequently led to the dissolution of the agreement. Many a pool has been wrecked by a desire on the part of its members to get rich too quick. Yet even if the pool did not raise prices so high as to invite competition, it proved very difficult to hold the pool intact during a period of declining demand. A reduction of output became imperative in order to maintain prices, yet this meant higher costs, because of the distribution of fixed expenses over a smaller output. Hence each member was tempted to sell more than the amount allotted to him. The only possible outcome was reduced prices. Thus, the experience of pools has generally been, that as a contrivance for restricting competition they are but temporarily successful. (2) Pooling agreements were and had long been at variance with the common law. According to the common law pools were negatively illegal, i. e., they were merely nonenforceable in the courts. Even therefore before by the Sherman Act of 1890

they became positively illegal,[1] resort was had in some industries to a new device for restraining competition—the trustee device. A description of this new expedient will form the subject of the next chapter.

[1] Railway pools were made illegal by the Act to Regulate Commerce of 1887.

CHAPTER III

THE TRUSTEE DEVICE

The first resort to the trustee device or the "trust," as it will be called to distinguish it from the modern trust, was by the Standard Oil Company. Prior to 1879 Mr. John D. Rockefeller and his associates had acquired a large number of oil concerns in the interest of the Standard Oil Company, but the shares of these concerns (instead of being held directly by the Standard Oil Company) had been registered in many cases in the names of various individuals who held them for the benefit of the company. In order to centralize more fully the control of these properties, it was decided in 1879 to organize the Standard Oil "trust."

The "trust" agreement as revised in January, 1882, included about forty companies, controlling from 90 to 95 per cent of the refining capacity of the country.[1] It provided for nine trustees, among whom were Messrs. John D. Rockefeller, William Rockefeller, H. M. Flagler, and John Archbold. The trustees received from each of the parties to the agreement an assignment of their stock with voting power, and in return therefor gave "trust certificates" representing the valuation of the properties. The trustees did not become the owners of the stocks deposited with them; they simply held them in trust for the owners of the trust certificates. It should be noted, however, that these stocks were held by the trustees for the joint account rather than for the individual account of the certificate holders; a stockholder in any one company lost by the trust agreement his title to the stock of that particular company, and secured instead a proportionate

[1] Brief for the United States in Standard Oil Company *v.* United States (no. 725), vol. I, p. 48. A copy of the agreement is in the Report of the Commissioner of Corporations on the Petroleum Industry, part I, pp. 361–370.

interest in all the stocks and property held by the trustees.[1] The trustees together owned 466,280 of the trust certificates out of a total of 700,000; and four of them held a majority of the trust certificates. They were thus able to elect the officers and directors of each of the constituent companies, and to manage the properties in complete harmony.

The trustees under this agreement were given powers substantially similar to those possessed by the directors of an ordinary holding company. They were to collect the interest and dividends on the securities held in trust, and to redistribute such portion thereof as they saw fit among the holders of the trust certificates. They were authorized to use any surplus trust funds to purchase the bonds and stocks of other companies engaged in the oil business, and to hold these securities for the benefit of the trust certificates. The centralized control provided for in the agreement made it possible for the trustees to dismantle those refineries that were poorly located, and to build new works at strategic points. Obviously it made no difference to the former owners of a given plant whether or not that plant was operated, since they received a certain percentage of the profits earned by all the companies. The trust agreement, further, made provision for the admission of new companies and individuals; for the formation, whenever advisable, of a Standard Oil Company in any state in the country. The duration of the agreement was to be for a period of twenty-one years after the death of the last surviving trustee, but provision was made for the termination of the agreement within one year of its execution upon the approval of nine-tenths of the certificates (in value), and within ten years upon the approval of two-thirds of the certificates.

The success of the Standard Oil "trust" invited imitation. In 1884 there was formed the American Cotton Oil "trust"; and in 1885 the National Linseed Oil "trust."[2] The cotton oil

[1] This consideration proved to be highly important when the "trust" was dissolved in 1892. See p. 25.

[2] Conant, Publications of the American Statistical Association, 7, p. 208 (March, 1901).

"trust" included some seventy mills, located for the most part in the South, engaged in manufacturing and refining cotton seed oil.[1] Its form of organization was precisely like that of the Standard. However, it soon met with difficulties on all sides, and in 1889 was reorganized as the American Cotton Oil Company.

In 1887 a "trust" was organized in the whisky business. From 1882 to 1887 some eighty distillers had maintained a precarious existence through pools. These pools, however, had proven unsatisfactory; it had not been possible to maintain them. Accordingly the leading distillers decided to establish a more compact organization modelled on the Standard Oil trust agreement of 1882. This was accomplished in May, 1887.[2] The Distillers and Cattle Feeders' Trust, as the new organization was called, comprised about eighty companies, located mainly in New York, Ohio, Indiana, Illinois, Wisconsin, Missouri, and Nebraska, manufacturing from 85 to 90 per cent of the total output of alcohol and spirits. There were nine trustees, who issued trust certificates in exchange for the shares of the corporations entering the "trust." Inasmuch as the trustees held a majority of the stock of every corporation, they were able to elect the directors and officers, and thus to control the management. This in turn enabled them to control the market, for instead of exporting the surplus at a loss, as had been done by the earlier pools, it was now possible to limit the output to the demand. It also lay within the power of the trustees to close up the poorest distilleries; and they did close some sixty-eight of them, the output being concentrated in the best equipped plants, with a consequent saving in the cost of production.

Another group resorting to the trustee device was the sugar refiners. During the seventies and eighties competition in the sugar refining industry had been quite keen; between 1867 and 1887 some thirty-six refineries had been closed.[3] By 1887 there

[1] Andrews, Quarterly Journal of Economics, 3, p. 129.

[2] A copy of the agreement is in House Report no. 4165, 50th Cong., 2nd Sess., pp. 57 seq. See ibid., pp. 64, 72, 91; and Jenks, Political Science Quarterly, 4, pp. 305–308.

[3] Cf. Jones, Quarterly Journal of Economics, 34, p. 505.

were left only twenty-six refineries, operated by twenty-three companies. The concerns that survived this period of severe competition were those that resorted to large-scale production, with its resulting economies. In August, 1887, seventeen of these companies, owning twenty refineries, and possessing among them approximately 78 per cent of the refining capacity, entered into a trust agreement to become effective October 1, 1887.[1]

In its main provisions this agreement was substantially like the trust agreements already described. Eleven trustees constituted a Board, known as the Sugar Refineries Company, and distributed trust certificates ($50,000,000) to the shareholders of the corporations in return for the securities held by them. The trustees thereupon caused themselves or their representatives to be elected directors of the separate corporations, and were thus able to manage the affairs of all in unison. It was provided that 15 per cent of the certificates allotted to the several companies should be left with the Board, and that these and any part of the $50,000,000 of certificates not allotted might be employed by the Board for the acquisition of other refineries or for certain other purposes. A unique feature of the sugar trust deed was a provision that no trustee should be interested directly or indirectly in the purchase or sale of sugar, whether for the purpose of speculation or otherwise, without the consent of a majority of the Board. Of the twenty refineries acquired by the Sugar Refineries Company twelve were soon dismantled, and the other eight were consolidated into four.

In this same year (1887) there was organized the National Lead Trust [2] and the Cordage "trust."[3] The latter, known as the National Cordage Association, controlled at this time only 30 per cent of the country's output of rope and cordage; it was

[1] Original Petition in United States *v.* American Sugar Refining Company, pp. 38–40, 166. For a copy of the trust agreement, see ibid., exh. A.

[2] Conant, Publications of the American Statistical Association, 7, p. 209 (March, 1901).

[3] Dewing, Corporate Promotions and Reorganizations, pp. 116–117, 120–121.

not until 1891 that it attained a monopolistic position in the industry.

The organization of these "trusts" was followed by a general outcry against monopolies. How fully the attention of the public had been called to the establishment of the "trusts," and what its reaction was, is shown by the numerous laws forbidding combinations and trusts enacted by the state legislatures from 1889 to 1893,[1] and by the passage by the National Congress in 1890 of the Sherman Anti-trust Act, which prohibited every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several states, or with foreign nations, and every monopoly or attempt to monopolize. And as it soon proved, the "trusts" were particularly vulnerable, much more so than the pools. The pools, it is true, were unlawful, but they were secret agreements, and therefore were to some extent free from attack. The Addyston Pipe and Steel Company is the most conspicuous instance of a pool dissolved by legal process, and the evidence here was obtained only because a disgruntled stenographer painstakingly accumulated it. The trust agreements of the eighties, however, were tangible matters of record. There was a formal transfer by the stockholders of their legal title to the stock of the constituent companies, as a consideration for which they received trust certificates. The rights of the members were clearly defined in the trust agreement. The fact could not be concealed that these companies, whose corporate existence had been preserved, had almost completely sacrificed their independence.

Hardly had the "trusts" been created when legal proceedings were instituted against them. The state of Louisiana attacked the cotton oil "trust"; the state of Nebraska, the whisky "trust";[2] the state of New York, the sugar "trust"; and the

[1] At least six states—Kansas, Maine, Michigan, North Carolina, Tennessee, and Texas—passed such laws in 1889.

[2] See p. 312 for the decision of the Supreme Court of Nebraska; and p. 316 for the decision of the Supreme Court of Illinois declaring illegal both the whisky "trust" of 1887 and the corporation that succeeded in 1890 to its business.

state of Ohio, the oil "trust." The action against the sugar "trust" came in 1888. In that year the Attorney General of New York State brought suit under the common law against the North River Sugar Refining Company, a New York corporation, praying that the charter of the company be vacated and the company dissolved. In a decision rendered in June, 1890, the Circuit Court of Appeals decided against the company.[1] The court held that the North River Sugar Refining Company, in entering the "trust," had given over the control of its affairs to an irresponsible board, and that such delegation of its essential corporate powers was a perversion of the privileges conferred by the company's charter. Furthermore, the court held that the company had helped to create a trust which, in substance and effect, was a partnership of separate corporations, and for corporations to enter a partnership was illegal. The company's charter, therefore, was taken away, and its corporate existence terminated.

The Standard Oil "trust" agreement was likewise condemned by the courts. In May, 1890, the Attorney General of Ohio filed a petition against the Standard Oil Company of Ohio, charging that the company had violated the laws of the state by placing the control of its affairs in the hands of trustees, nearly all of whom were nonresidents of the state. Great pressure was brought to bear on the Attorney General to induce him to discontinue the suit, but without success. The decision of the Supreme Court was rendered in March, 1892.[2] As in New York State, the "trust" arrangement was declared illegal, though the Ohio court put more emphasis on the creation of a monopoly. The court said: "the observance [of this agreement] must subject the defendant [the Standard Oil Company of Ohio] to a control inconsistent with its character as a corporation. . . . The law requires that a corporation should be controlled and managed by its directors in the interests of its own stockholders, and confor-

[1] 121 N. Y. Reports 582–626. The decision is described in more detail on p. 313.

[2] 49 Ohio State Reports 137–189. For a fuller discussion of this decision, see p. 314.

mable to the purpose for which it was created by the laws of its state. By this agreement, indirectly, it is true, but none the less effectually, the defendant is controlled and managed by the Standard Oil Trust, an association with its principal place of business in New York City, and organized for a purpose contrary to the policy of our laws. Its object was to establish a virtual monopoly of the business of producing petroleum, and of manufacturing, refining and dealing in it and all its products, throughout the entire country, and by which it might not merely control the production, but the price at its pleasure. All such associations are contrary to the policy of our state and void." The court did not order the dissolution of the Standard Oil Company, as urged in the petition, but simply commanded it to cease its connection with the "trust."

Any expectation that the decision of the Supreme Court of Ohio would put an end to the oil monopoly proved to be unfounded when the nature of the dissolution became apparent. On March 21, 1892, at a meeting of the trust certificate holders, a resolution terminating the "trust" was adopted.[1] At this time the stocks of eighty-four companies were held by the Standard Oil trustees. On April 1 the stocks of sixty-four of these corporations were transferred to some one of the remaining twenty. This left the stocks of twenty companies in the hands of the trustees, and these they proceeded to distribute among the holders of the trust certificates. There were outstanding at this time $97,250,000 trust certificates. The trustees, who became liquidating trustees, divided the stock of each of the twenty companies into 972,500 parts. They then offered to give to each trust certificate holder in exchange for each share 1/972,500 part of the stock of each one of the twenty corporations. The only ones who accepted this offer were the trustees (themselves the largest certificate holders) and the members of their families and their immediate associates. The smaller trust certificate holders were discouraged from liquidating by the fact that they would have received only fractional

[1] On the dissolution scheme see Brief for the United States in Standard Oil Company v. United States (no. 725), vol. I, pp. 56–58, 60–61, 70, 72.

shares in the twenty companies, and these companies declined to pay dividends on fractional shares. Dividends continued to be paid, however, on the trust certificates when not liquidated. The nine trustees, therefore, became the holders of the majority of the stocks of the twenty companies, and as liquidating trustees they also held the stocks not exchanged for trust certificates. This dissolution obviously was nominal; it effected no real change in the situation. In fact, Mr. Archbold admitted before the Industrial Commission that the companies worked together after the dissolution as harmoniously as before.[1]

It was apparent that the Standard interests had not attempted to obey the court's order, but had stooped to a mere subterfuge. A new suit, therefore, was instituted in 1897 against the Standard Oil Company for failure to obey the court's decree of March, 1892. This suit dragged along until December, 1900, when it was dismissed. Meanwhile the Standard Oil Company had reorganized as a holding company.[2]

[1] I, p. 574.

[2] See p. 56.

CHAPTER IV

THE MODERN TRUST MOVEMENT

The decisions of the New York and Ohio courts in 1890 and 1892, respectively, showed that even without the prohibitions of the Sherman Anti-trust Act the "trust," so far as the law was concerned, was not a permissible form of business organization. The Standard Oil interests, it is true, avoided collision with the law for a time by the development of a community of interest, but this loose form of organization proved satisfactory mainly because there already existed among the members an unusual degree of mutual confidence and good will. It appeared, therefore, that unless some new expedient for restraining competition could be hit upon, the manufacturers insistent upon holding competition in check must needs resort once more to pooling agreements. Yet this was even less desirable than before from the manufacturers' standpoint, since the Sherman Anti-trust law had been passed in 1890. This act made pools, when effecting a restraint of trade, not only unenforceable, as under the common law, but actually illegal; and their existence would therefore have to be kept secret. By what means then were the manufacturers to secure relief?

The new expedient to restrain competition was the modern trust. The trust was effected in one of two ways: either by means of a security holding corporation, that is, a company owning all or part of the securities of other companies; or by means of a property holding corporation, that is, a company owning outright the plants and other property of the companies to be united in the trust.

First. The holding corporation is a type of business organization employed to combine a group of corporations by owning all or a majority of the stock. The holding company, whether a newly created corporation or one already in existence, must

possess legislative authority to hold the stocks of other corporations. Armed with such authority it proceeds to purchase, either with cash or with its own securities, a majority at least of the shares of the companies which it plans to combine. The controlled companies maintain their separate existence, they have their separate officers and managers, and they are nominally independent; yet inasmuch as the holding company elects their directors, it can effectively control their management and operate their properties in accordance with a unified plan.

The holding corporation was thus after all but a modification of the illegal "trust" which it was designed to supersede. As Professor Meade has pointed out,[1] the only important changes effected were: the substitution of the shares of the holding company for the certificates of the old "trust"; the substitution of the relation of owner for the relation of trustee; and the substitution of a board of directors for a board of trustees. It would appear therefore that from the point of view of legal principle the new arrangement was quite as unlawful as the old.

What then, it may be asked, was to be gained by adopting the new form of organization? The possible gain was two-fold. From a legal point of view the holding company might prove less vulnerable. The old "trust" was an agreement between a body of trustees and a group of corporations, which, through the action of a majority of their stockholders, surrendered their independence, and in so doing exceeded their corporate powers. The holding company, however, was authorized by law to hold the securities of other companies. As a device for restraining competition it had not yet been declared illegal, and there was at least the possibility that it might successfully withstand an attack upon its validity. Yet even if ultimately its fate did prove to be that of the "trust," a second gain was possible. The organization of the holding company insured a temporary respite from competition, and presumably the profits thus realized would be retained by the corporation or its stockholders, and would not need to be returned to the consumers from whom

[1] Trust Finance, p. 36.

they had come. Barring heavy penalties for the employment of an illegal device, there was much to gain in the organization of a holding company trust and little to lose.

If the holding company as a means of eliminating competition presented such attractive possibilities, why was it not adopted earlier? The reason is that no express legislative sanction existed for the creation of a holding company.[1] The power to buy and sell the stocks of other corporations, like all other corporate powers, is one derived from legislative authority; and during the period when "trusts" were being formed (1879–1887) no state had passed a general law specifically granting this privilege. Such few holding companies as existed had been created under special laws. One of the first holding companies of any consequence to be authorized was the Pennsylvania Company, chartered in the interest of the Pennsylvania Railroad Company in 1870, and empowered "to make purchases and sales for investments in the bonds and securities of other companies." The reason for this special enactment was to permit the Pennsylvania Railroad to centralize the control of certain lines that were closely affiliated with it.[2]

An arrangement of somewhat the same sort was made use of by the Philadelphia and Reading Railway in the early seventies. This railway was anxious to possess anthracite coal properties in order to insure an ample coal traffic for the future. Under its charter, however, it had no authority to own coal lands. It therefore had incorporated in its interest the Laurel Run Improvement Company, which was authorized by its charter to buy coal lands and to mine coal. The charter further provided that the stock of this mining company might be acquired by any Pennsylvania railroad or mining company. Thereupon the Philadelphia and Reading Railway proceeded to buy all the coal company's stock, and thus indirectly it secured the power to act as a holding company in this particular instance.[3]

Save for some such exceptional cases as these, the holding by

[1] Noyes on Intercorporate Relations (second edition), secs. 5, 264 ff.
[2] See Annual Report of the Pennsylvania Railroad, 1871, p. 19.
[3] Jones, The Anthracite Coal Combination in the United States, p. 30.

one corporation of stock in another corporation was not legal,—or at least had not been so held by the courts. And in view of the popular hostility towards trusts, which resulted in a wave of anti-trust legislation after 1889, it was hardly to be expected that any state would go out of its way to extend assistance to those who were searching for a new device to legalize their operations. The unexpected, however, came to pass. It was the state of New Jersey that came to the rescue.

Whether or not the legislators realized the full significance of their action,[1] the state of New Jersey amended its corporation law in May, 1889, and provided that the directors of any company organized under the act of 1875 might purchase "the stock of any company or companies owning, mining, manufacturing or producing materials, or other property necessary for their business," and issue its own stock in payment therefor.[2] Four years later, in 1893, the doors were thrown completely open to the creation of holding companies by the enactment of a provision that any corporation might purchase and hold the securities of any other corporation no matter in what state incorporated, and might, while the owner, exercise all the rights of ownership.[3] No operating duties were required of the holding company; its duties were simply the ownership of stock, the election of officers and directors, the receipt of dividends from the constituent companies, and the payment of these dividends in whole or in part to its own stockholders.

[1] The charge has been made that some of the trusts "are a product of legislation obtained by their own lawyers and legislative agents, put quietly through under the cover of the anti-trust agitation, while the public, led by the newspapers, were looking somewhere else." Whitney, former Assistant Attorney General of the United States, Publications of American Economic Association, 3rd series, vol. 6, part II, p. 4 (Papers and Proceedings).

[2] Dill, The Statute and Case Law of the State of New Jersey relating to Business Companies (1910), p. 80.

[3] Dill, op. cit., p. 80. The section in full read: "Any corporation may purchase, hold, sell, assign, transfer, mortgage, pledge or otherwise dispose of the shares of the capital stock of, or any bonds, securities, or evidences of indebtedness created by any other corporation or corporations of this or any other state, and while owner of such stock may exercise all the rights, powers and privileges of ownership, including the right to vote thereon."

The example set by New Jersey was soon followed by other states determined to prevent New Jersey from securing a monopoly of incorporation fees and other fees and taxes. Among the numerous states that revised their general corporation laws to permit the creation of holding companies were Delaware, Maine, West Virginia, and New York, these states being conspicuous for the "liberal" character of their legislation.[1]

One of the first companies to avail itself of the New Jersey legislation was the American Cotton Oil "Trust." Fearing lest the "trust" should prove illegal, it reorganized in New Jersey in October, 1889, as the American Cotton Oil Company, a holding company possessing the stocks of sixteen constituent concerns.[2] The American Cotton Oil Company also operated a large refinery in New Jersey on its own account, but it was primarily a holding company.

In spite of the advantages of the holding company plan, however, few concerns availed themselves at once of the opportunity thereby afforded of organizing a trust. Thus, the Standard Oil "trust," though declared illegal in 1892 and obliged to reorganize, did not seek refuge in New Jersey, but relied instead on the community of interest plan. That more New Jersey holding companies were not formed is partly explained by the unsatisfactory state of business during the early life of the law, the period from 1893 to 1897 being one of severe industrial depression, when the flotation of new issues of securities would have proved difficult; and partly by the fact that use was made of the other method of forming a modern trust, namely, the *property* owning corporation.

Second. Most of the trusts or attempted trusts organized in the years immediately following the court decisions declaring the "trusts" or "trust" agreements illegal, took the form, not of a security holding company, but a property holding company. This second type of trust came into being in at least three

[1] The statutes of the different states authorizing corporations to acquire stock in other corporations are given in Noyes on Intercorporate Relations (second edition), sec. 271.

[2] Industrial Commission, XIII, p. 680.

different ways: (1) by means of a consolidation or merger; (2) by means of purchase and sale; and (3) by means of exchange of property for stock.[1]

(1) Consolidation or merger may be defined as the union in one corporate body of two or more existing corporations.[2] In effecting a consolidation the property and business of one or more companies is turned over to the consolidated company, whether or no this be a newly created corporation or one already existing.[3] By the act of consolidation the separate companies completely lose their identity, unless indeed their existence is maintained for some special purpose, such as the adjustment of claims.[4] The

[1] In common usage the terms "purchase" and "sale" are applied to the acquisition by one corporation of the property of others in exchange for its stock (see Noyes on Intercorporate Relations, second edition, sec. 319); and it may be, therefore, that our classification of property owning trusts is more minute than is necessary.

[2] Some legal authorities make a distinction between a consolidation and a merger. Thus, Thompson, Law of Private Corporations (second edition) says, "there seems to be a recognized difference between 'consolidation' and 'merger'" (sec. 6035). "Consolidation takes place where two or more existing corporations are consolidated into a single corporation, and the existence of the uniting corporations is terminated and the consolidated company succeeds in a general way to the rights and franchises and acquires the property and assumes the obligations and liabilities of all the constituent companies" (sec. 6035). A merger, on the other hand, "exists where one of the constituent companies remains in being, absorbing or merging in itself all the other companies" (sec. 6037). But in Judicial and Statutory Definitions of Words and Phrases, 1914, p. 908, we are told that the terms consolidation and merger are not always used with strict accuracy. As one authority puts it (ibid., 1904, p. 1452), the term consolidation is an elastic one, and may include a union of two or more corporations into a new one with a different name, with or without extinguishing the constituent corporations, or the merging of two or more corporations into one existing corporation under the name of the latter. See also Noyes on Intercorporate Relations (second edition), secs. 7–8. For our purposes there is nothing in particular to be gained by determining whether the property of the companies combined has been turned over to a new corporation or has been acquired by an already existing corporation; and we shall therefore use the words consolidation and merger interchangeably.

[3] See footnote above.

[4] Thompson on Corporations (second edition), sec. 6041.

consolidation thus represents the complete fusion of two separate businesses.

A consolidation is ultra vires unless authorized by legislative authority; and the legislature may withhold its consent entirely, or it may permit consolidation upon such conditions as it chooses to impose.[1] Legislative approval of consolidation may be given in various ways.[2] The legislature may provide for consolidation under a general corporation law; and most states through such laws now permit the formation of consolidations for lawful purposes. It may grant the constituent companies charters permitting consolidation under certain conditions. It may even give its approval after the fact by the recognition of the consolidated corporation; and such legislative recognition is equivalent to legislative ratification. When the corporations to be consolidated are creatures of different states the approval of each separate state, by general law or otherwise, is necessary to make the consolidation valid.[3]

Yet even if the legislature has given its assent, no corporation can consolidate with another without the consent of the stockholders. If the charter of a company gives it authority to consolidate, or if any general law in force at the time when the company was chartered permits consolidation, only the consent of a majority of the shareholders is required; otherwise the consent of all the shareholders is necessary.[4] A dissenting stockholder in the latter case can not be compelled to give his assent, and his consent can not be implied.

When the consent of the legislature and of the stockholders has been secured, the process of effecting a consolidation, as already pointed out, is for the separate companies to transfer their property and assets to the consolidated company, whereupon they become extinguished.[5] The consolidated company is thus an operating unit, in contrast with the

[1] Thompson on Corporations (second edition), secs. 6043, 6045.

[2] Noyes on Intercorporate Relations (second edition), sec. 20.

[3] Ibid., sec. 100.

[4] Morawetz on Private Corporations, sec. 951.

[5] Unless one of them becomes the consolidated company.

holding company, which ordinarily is not an operating unit at all.[1]

(2) Purchase and sale. "It is an elementary principle of corporation law that a corporation, subject to the limitations of its charter and constitutional and statutory prohibitions, has inherent power to acquire and hold any property, real or personal, reasonably useful or convenient in carrying on the business for which it was organized." [2] A private corporation—but not a quasi-public corporation, such as a railroad—may even dispose of its entire property with the unanimous consent of the stockholders, providing the purpose is not unlawful nor fraudulent. If within the powers expressly granted to it, it may accept stock in other corporations in payment for the property sold. If the corporation whose property is to be disposed of is a losing one, the consent of only a majority of the stockholders suffices; and this is also true in the case of a prosperous corporation, when the sale of its entire assets is made for legitimate business reasons.[3] Though some trusts were organized through sales to them of corporate property, it is hardly necessary to point out that such sales, if made for an unlawful purpose, were ultra vires of the corporation.

It is necessary to distinguish between a sale and a consolidation. In a sale the vendor parts solely with its property, for which it receives a quid pro quo. The vendor may then proceed to buy further property, if it desires. But in a consolidation the vendor not only parts with its property, but also with the legal right to own or acquire property. Obviously the vendor could not receive any consideration for the transfer; for the act of consolidation involves its extinguishment. The fact that the consolidated company makes payment, not to the vendor corporation, but to its stockholders, characterizes the transaction as a consolidation rather than a purchase; if the trans-

[1] For an excellent statement of the law relating to consolidation of corporations, see Noyes on Intercorporate Relations (second edition), secs. 7–107.

[2] Noyes on Intercorporate Relations (second edition), sec. 108. On the subject of sales of corporate property, see ibid., secs. 108–117.

[3] See Warren, Harvard Law Review, 30, p. 358.

action were merely a purchase and sale, the company acquiring property would pay the vendor corporation, which would then settle with its stockholders.

(3) Exchange of property for stock.[1] A private corporation may not only sell its entire assets, as just explained, but it may also exchange its assets for any other property that it is empowered to acquire. If the vendor corporation has power to hold stock in another corporation, it may transfer its property to the proposed trust, and receive its stock in exchange. Such an exchange differs from a sale in this respect, inter alia, that a sale of the entire property, when incident to dissolution, may be accomplished on occasion through a majority vote; whereas an exchange of the entire property for stock requires the unanimous consent of the stockholders; the majority cannot force the minority into a new company against its will.

The stock received in the process of exchange belongs, of course, to the corporation that has transferred its property. But the corporation, with the unanimous consent of its stockholders, may enter into an agreement that the stock, instead of being delivered to it, shall be distributed among its stockholders pro rata. Such an agreement is the equivalent of a liquidation of the company's business by unanimous consent, but in the absence of statutory provisions to the contrary is a valid arrangement.

On some occasions property owning trusts were formed through the use of the holding company as an intermediary stage. The holding company having acquired a majority or all of the stock of the constituent companies was obviously in a position, particularly if it had acquired all of the stock, to cause the underlying property to be conveyed to it, and the separate companies to be dissolved. Upon the completion of these transactions the trust owned, not stocks, representing the title to plants, but the plants themselves.

The formation of a trust through the exchange of its stock for the property of the companies to be united would appear to have been provided for at an early date by the same New Jersey law

[1] On this subject see Noyes on Intercorporate Relations (second edition), secs. 118–129a.

to which reference has already been made.[1] By an amendment to section 55 of its general incorporation law of 1875 the state of New Jersey in 1889 authorized the directors of any company incorporated under the act to purchase mines, manufactories, and other property necessary for their business, and to issue stock in payment therefor.[2] Apparently New Jersey was not influenced by the popular clamor against trusts, and did not propose to stop at halfway measures of protection.

The American Tobacco Company, incorporated in New Jersey in 1890, illustrates a property owning trust, as distinct from a holding company trust. This company, among the first of the modern trusts, exchanged its capital stock directly for the plants, business, brands, and good will of five cigarette companies.[3] The Continental Tobacco Company (the plug tobacco trust), organized in New Jersey in 1898, was the same type of trust,[4] as was also the second American Tobacco Company, organized in 1904 for the purpose of uniting a number of tobacco concerns (including the original American Tobacco Company and the Continental Company) that had been held together since 1901 through the Consolidated Tobacco Company (a holding company).

The American Sugar Refining Company, incorporated in New Jersey in 1891, is another early property owning trust.[5] The Sugar Refineries Company (the "trust") having been declared illegal, the trust certificates, by agreement among all the parties, were exchanged for the shares of the American Sugar Refining Company. Through the acquisition of these trust certificates, the American Sugar Refining Company

[1] See p. 30.

[2] See the General Law of the State of New Jersey concerning Corporations, approved April 7, 1875, together with Acts Amendatory thereto in force July 1, 1889, p. 34.

[3] Report of the Commissioner of Corporations on the Tobacco Industry, part I, p. 65.

[4] Report of the Commissioner of Corporations on the Tobacco Industry, part I, pp. 99–100.

[5] Original Petition in United States *v.* American Sugar Refining Company, pp. 47–50.

secured control over all the stock of the various corporations formerly controlled by the trustees. It was thus temporarily a holding company. The next step was to have the several corporations convey to it their entire property, whereupon they were dissolved. The result was to make the American Sugar Refining Company the actual owner of all the property previously held in trust by the trustees under the Sugar Refineries Company deed.

In passing, the relative merits of holding company trusts and property owning trusts from the standpoint of trust managers may be briefly reviewed.[1] The chief advantages of the holding company are: (1) it makes possible the creation of a centralized administration, and yet at the same time maintains the individuality of the constituent companies, together with the good will attaching to their business; (2) through the incorporation of individual concerns in the separate states, it is able more easily to comply with the laws of the various states, such as, for example, a law that foreign corporations may not hold real estate; and (3) it is easy to form, because it is necessary to acquire only a majority of the stock of the separate companies.

On the other hand, it is open to serious objections: (1) the perpetuation of the individual concerns whose stock is acquired results in the creation of a complex business and financial structure, a set of wheels within wheels, that does not conduce to the maximum operating and financial efficiency; and (2) in case all the stock of the constituent concerns is not acquired, the control of the business through the ownership of only a part of the stock separates control from ownership in large measure, and is thus likely to give rise to the manipulation of accounts, and to the sacrifice of one set of stockholders in the interests of another, with resulting dissatisfaction and friction.

The advantages of a trust that owns the property outright are: (1) it provides a unified operating unit with a resulting concentration of power and responsibility—under this type of trust it is possible to dispense with a lot of individual companies, each

[1] For an excellent discussion at greater length, see Haney, Business Organization and Combination (1915), chs. 15–16.

having its own officials and organization, and to substitute therefor a single concern dominated by singleness of purpose; and (2) by uniting all the property in one concern it makes the interests of each the interests of all, and thus eliminates that "milking" of one group by another which occurs not uncommonly under the holding company device. The disadvantages are: (1) it sacrifices the independence of the separate concerns, and thus their franchises and firm names; (2) it can not accommodate itself so readily to local conditions; and (3) it is more difficult to form, because of charter and statutory restrictions. Nevertheless, as we shall see, trusts more generally took this form rather than the holding company form.

The general character of the trust movement has been indicated. There remains to consider its extent.

The extent of the movement toward *combination* can be statistically stated with a fair degree of precision, and several such compilations are available.[1] A similar statistical study of the *trust* movement, however, can not be made by an independent investigator; to secure the requisite data in fullness requires the resources and authority of a governmental agency. To discover and enumerate all the combinations of a certain size (say capitalization) is easy; but to determine in each instance whether the combination realized monopoly control (that is, was a trust) is quite another matter. The attempt to make such a computation is rendered more difficult by the fact that a combination at its organization may not possess monopolistic powers, but subsequently may acquire them. The National Cordage Company is a case in point. It has seemed best, therefore, to indicate the extent of the trust movement by using the statistics for the combination movement, with a caution against a too literal interpretation of the figures as bearing on the trust movement.

An excellent statistical study of the industrial combinations formed in the United States through 1900 has been made by Mr.

[1] See, for example, Conant, Publications of the American Statistical Association, 7, pp. 208–217 (March, 1901); U. S. Census, 1900, vol. 7, pp. LXXXVI seq.; and Moody, The Truth about the Trusts, pp. 453 seq.

Luther Conant, subsequently Commissioner of Corporations.[1] The following table, prepared by him, shows the number of industrial combinations, with a capital of $1,000,000 or over, effected from 1887 to 1900, with their authorized capitalization:

Year	*Number of combinations*	*Total capitalization, stocks and bonds*
1887	8	$216,226,000
1888	3	23,600,000
1889	12	152,179,000
1890	13	155,156,000
1891	17	166,200,000
1892	10	193,412,000
1893	6	239,015,000
1894	2	30,400,000
1895	6	107,255,000
1896	5	49,850,000
1897	4	81,000,000
Total (1887–1897)	86	$1,414,293,000
1898	20	$708,600,000
1899	87	2,243,995,000
1900	42	831,415,000
Total (1898–1900)	149	$3,784,010,000
Total (1887–1900)	235	$5,198,303,000

During the eleven years 1887–1897, therefore, there were formed 86 industrial combinations with an authorized capital of $1,414,000,000. Some of these combinations were trusts also, that is, they exercised monopolistic control over the industry; but by far the greater number were simply combinations. The list includes five brewing companies, each a combination, but none of them a trust; and the whisky trust in its various forms is counted three times. The list includes the sugar trust twice, once as the Sugar Refineries Company, and again as the American Sugar Refining Company. It includes four steel companies, none of which was a trust. The number of actual

[1] Publications of the American Statistical Association, 7, pp. 207–226 (March, 1901).

trusts formed from 1887 (the date of the formation of the last "trust") to 1897 is thus considerably less than the number of combinations. Probably not more than twenty, or at most twenty-five, of these combinations secured a sufficient control of the industry to be called trusts.

Among the more important trusts formed between 1887 and 1897 were the following: National Cordage Company (1887); American Cotton Oil Company (1889); Diamond Match Company (1889);[1] American Tobacco Company (1890); Distilling and Cattle Feeding Company (1890); National Starch Manufacturing Company (1890); American Sugar Refining Company (1891); National Wall Paper Company (1892); United States Leather Company (1893); American Malting Company (1897); and Glucose Sugar Refining Company (1897).[2]

Nearly all of these trusts represented combination by consolidation or purchase rather than by means of a holding company. The cordage, match, cigarette, whisky, starch, sugar, leather, malt, and glucose trusts were property owning combinations. The cotton oil trust, on the other hand, was a holding company. No doubt there were others that took this form also, though the paucity of data on this subject makes it difficult to determine just which ones they were.

The real trust movement, however, dates from 1898. This is indicated by the statistics for combinations. Reference to the table on page 39 shows that in the years 1898 to 1900 there were formed 149 combinations, with a total capital of $3,784,000,000. In three years almost twice as many combinations were formed as in the preceding eleven years; and the capital of the combinations organized during the shorter period exceeded by more than two and one-half times the capital of those organized during the longer period. In the year 1899 alone, when the trust movement reached its climax, more combinations with a much larger aggregate capitalization were formed than in the eleven

[1] This company, incorporated in Illinois, was a successor to another company of the same name incorporated in Connecticut in 1880 for the purpose of monopolizing the match industry. See 77 Michigan Reports 635.

[2] Seven of these eleven trusts were chartered in New Jersey.

years from 1887 to 1897. The absorption of this mass of securities proved to be such an enormous task that in the latter part of 1899 and in 1900 the promoters had difficulty in inducing the bankers to float and the public to buy new issues. Nevertheless, 42 combinations with a combined capitalization of $831,000,000 were formed in 1900.

As in the period 1887–1897, by far the greater number of these combinations were simply combinations; they did not result in the formation of an organization large enough to control the industry. In the list of 149 combinations, we find, for example, seventeen in the steel industry. Several of these unquestionably possessed a degree of monopoly control over certain kinds of steel products—the American Steel and Wire Company of New Jersey, the American Tin Plate Company, the National Tube Company, and the Shelby Steel Tube Company are properly designated as trusts. But just as clearly, certain other of these steel combinations were in no sense trusts. This was true of the Empire Steel and Iron Company, the Republic Iron and Steel Company, the Sloss-Sheffield Steel and Iron Company, Jones and Laughlin, and several others; and was even true of such enormous combinations as the Federal Steel Company, the National Steel Company, and the Carnegie Company, each a vigorous competitor of the others, as subsequent events well demonstrated. We also find in our list of combinations nine in the liquor trade, in addition to those effected prior to 1898. For the most part these were merely local combinations. In addition there were four tobacco combinations, three brick and three fertilizer combinations, and two ice and two biscuit combinations. Most of these concerns obviously were not trusts. Though most of the companies promoted from 1898 to 1900 were simply combinations, it is still true that this was the period during which the modern trust movement reached its height. Some forty to fifty of these combinations achieved a monopolistic position in their particular industry; and this was approximately —an approximate statement is all that can be made—twice the number of trusts organized during the preceding eleven years.

Some of the leading trusts organized during 1898–1900 were:

the American Tin Plate Company (1898); Continental Tobacco Company (1898); International Silver Company (1898); International Paper Company (1898); American Linseed Company (1898); Otis Elevator Company (1898); Standard Oil Company of New Jersey (1899);[1] United Shoe Machinery Company (1899); American Steel and Wire Company of New Jersey (1899); National Tube Company (1899); American Bicycle Company (1899); American Chicle Company (1899); Asphalt Company of America (1899); National Glass Company (1899); National Salt Company (1899); Standard Sanitary Manufacturing Company (1899); New England Cotton Yarn Company (1899); Mount Vernon-Woodberry Cotton Duck Company (1899); American Sheet Steel Company (1900); Shelby Steel Tube Company (1900); and American Snuff Company (1900).[2] By no means all of these companies retained their monopolistic hold for any considerable time, yet all of them either at their organization or shortly thereafter exercised monopoly control.

There were other trusts established during this period that were so notably unsuccessful that one hesitates to class them with the above. Among them were the following: National Shear Company (1898); United States Envelope Company (1898); American Hide and Leather Company (1899); and American Writing Paper Company (1899). Indeed some of the trusts in the earlier list might well be placed in this group, particularly the American Bicycle Company, the National Salt Company, the New England Cotton Yarn Company, and the Mount Vernon-Woodberry Cotton Duck Company.

Comparatively few of the trusts formed between 1898 and 1900 were holding companies. The most striking exception was the Standard Oil Company of New Jersey, which adopted the holding company plan as a substitute for the community of interest arrangement that had been in force since 1892, but which it seemed wise to abandon in 1899 in view of the attacks being made upon it by the state of Ohio.

[1] Reorganization as a holding company.

[2] Eighteen of the twenty-one trusts enumerated above were incorporated in New Jersey.

Even after 1900, when there was somewhat of a lull in the trust movement, the formation of trusts continued on a large scale up to 1904. A table prepared by Mr. John Moody gives a list of the combinations organized to 1904.[1] From this table it appears that 46 combinations (each with an outstanding capital of $1,000,000 or over) were formed in 1901; 63 in 1902; and 18 in 1903, making a total of 127 during the three years. If we note that Mr. Moody's list is not as exhaustive as Mr. Conant's,[2] it would appear that substantially as many combinations were formed during the three years from 1901 to 1903 as during the three years from 1898 to 1900. A detailed study of the combinations organized between 1901 and 1903, however, reveals the fact that they were mainly combinations of limited scope; the number of them that were trusts was distinctly less than in the preceding three-year period. Hardly more than twenty of them were trusts, as compared with some forty or fifty during 1898 to 1900. The leading trusts organized between 1900 and 1903 were: the United States Steel Corporation (1901); American Can Company (1901); International Harvester Company (1902); Corn Products Company (1902); and International Nickel Company (1902).[3] During this period also a number of important reorganizations took place. The Consolidated Tobacco Company was formed in 1901 to unite, through the holding company arrangement, the American Tobacco Company (the cigarette trust) and the Continental Tobacco Company (the plug tobacco trust). Other companies that represented trust reorganizations of one kind or another were: Eastman Kodak Company (1901); International Salt Company (1901); United States Cotton Duck Corporation (1901); Distillers Securities Corporation (1902); American Coal Products Company (1903); General Asphalt Company (1903); E. I. du Pont de Nemours Powder Company (1903); Pope Manufacturing Company of New Jersey (1903).[4]

[1] The Truth about the Trusts, pp. 453–467.

[2] For example, Mr. Conant included all combinations having an *authorized* capital of $1,000,000 or more, whereas Mr. Moody included only those having an *outstanding* capital of this amount.

[3] All of these five trusts were incorporated in New Jersey.

[4] A reorganization of the American Bicycle Company.

In 1903 a merger of the leading meat packers was proposed, but it did not come to pass. Instead the National Packing Company was organized, and through it a community of interest was effected, or, perhaps one should say, maintained.

The organization of trusts seems to have come rather definitely to an end by the close of 1903. The stock market panic of 1903, ascribable to the large mass of "undigested securities"; the popular opposition to trusts that was reflected in the creation of the Bureau of Corporations in 1903, the Northern Securities decision in 1904, casting by implication grave suspicion on the legality of trusts—all combined to dull the public appetite for trust stocks, and thus to make their manufacture no longer particularly profitable. Moreover, by the close of 1903, most of the industries that were at all adapted to monopolization, and many that were not, had been "trustified"; and accordingly the period that followed was mainly characterized by the endeavor, often unsuccessful, of the trusts to hold the position they had gained.

Whereas up to 1900 the most common form of trust organization was a single corporation owning the various properties outright,[1] after 1900 and up to the Northern Securities decision the holding company form vied with it in popularity. The steel trust was a holding company trust; the cigarette and plug tobacco trusts were tied together through a holding company; and holding companies were made use of in the gunpowder, whisky, and meat industries. On the other hand the harvester, tin can, and glucose trusts took the property owning form; and the powder trust proceeded to substitute this form for the holding company. But in 1904 the Supreme Court in the Northern Securities case [2] held the combination of two competing railroads through a holding company to be illegal, and thereafter the other type of organization came into renewed favor. In the tobacco industry, for example, there was straightway formed the second American Tobacco Company, which proceeded to acquire the property of the concerns formerly controlled by the

[1] See Industrial Commission, I, p. 10 (Review of Evidence).

[2] See p. 399.

Consolidated Tobacco Company, the holding company organized in 1901. Yet the property holding corporation, like the holding company, could not pass the legal tests, when entered into, as in this instance, to effect an illegal object. In 1911 the Supreme Court held the tobacco merger illegal. In the same year the Supreme Court adjudged the Standard Oil Company of New Jersey illegal, not because it was a holding company, but because it had effected a restraint of trade. From these decisions it clearly appears that neither the holding company nor the merger is legal, when used to effect an illegal object.

CHAPTER V

THE STANDARD OIL COMPANY [1]

Mr. G. H. Montague in the preface of his book "The Rise and Progress of the Standard Oil Company" observes that the oil business, in its early phase, was the reflex of prevalent railway methods, and that it is not fair to attempt to judge the situation without first ascertaining the standards set by the railway management of the time. It does not fall within the province of this treatment to judge the Standard Oil Company, but merely to point out some of the methods by which it acquired its power.

The first successful oil well was drilled at Titusville, Pennsylvania, in 1859. This great event was followed by the discovery of other oil deposits, and by the rapid development of the demand for refined petroleum products. At that time Mr. John D. Rockefeller, only twenty years of age, was engaged in the produce commission business on the Cleveland docks. But Mr. Rockefeller early foresaw the possibilities in the oil business, and in 1862 he and his partner, who had made excellent profits in the

[1] On the Standard Oil Company see: Report of the Commissioner of Corporations on the Transportation of Petroleum, May 2, 1906; Report of the Commissioner of Corporations on the Petroleum Industry, part I, Position of the Standard Oil Company in the Petroleum Industry (May 20, 1907), and part II, Prices and Profits (August 5, 1907); Report of the Federal Trade Commission on Pipe-Line Transportation of Petroleum; Report of the Federal Trade Commission on Price of Gasoline in 1915; Brief for the United States, in two volumes, in Standard Oil Company *v.* United States (no. 725); Brief for Appellants (Standard Oil Company et al.), in two volumes, in Standard Oil Company *v.* United States (no. 725); 173 Fed. Rep. 177–200; 221 U. S. 1–106; House Report no. 3112, 50th Cong., 1st Sess.; Industrial Commission, vol. I, pp. 261–800; 49 Ohio State Reports 137–189; 218 Missouri Reports 1–507; Tarbell, The History of the Standard Oil Company, in two volumes; Lloyd, Wealth Against Commonwealth; Montague, the Rise and Progress of the Standard Oil Company. (For full titles see the Bibliography.)

produce business as the result of the unusual demands created by the Civil War, invested $4,000 in an oil refinery, which one Samuel Andrews was anxious to start. Mr. Andrews proved to be a mechanical genius, and the little refinery at Cleveland became quite profitable. In 1865 Mr. Rockefeller disposed of his interest in the commission house, and entered into a partnership with Mr. Andrews. The partnership of Rockefeller and Andrews associated itself also with Mr. William Rockefeller in the firm of William Rockefeller and Company, and this new firm built another refinery on property adjacent to the works of Rockefeller and Andrews. These two concerns then organized the firm of Rockefeller and Company, a selling agency with headquarters at New York City. Mr. Rockefeller was one of the first to see that by producing on a larger scale improvements in the process of refining could be brought about, and the by-products more effectively utilized. In 1867, therefore, the three Rockefeller firms united with the firms S. V. Harkness and H. M. Flagler into a new concern called Rockefeller, Andrews and Flagler.

In 1870 (June) the Standard Oil Company of Ohio was incorporated with a capital stock of $1,000,000. This company took over the properties of the partnership to which it succeeded. The Standard Oil Company was, even at this time, the largest oil concern in the country. It produced about 10 per cent of the country's output of refined oil.[1] But it operated no refineries outside of Cleveland, was not engaged in the production of crude oil, and had as competitors some 250 concerns.[2] By 1879, however, the Standard Oil Company, according to the statement of its officials, controlled from 90 to 95 per cent of the refining business of the country.[3] By what means was a company occupying such a modest position in 1870 able so effectively to eliminate its competitors? According to the Commissioner of Corporations, "unquestionably, the most important single element in this early extension of the company's power

[1] Report of the Commissioner of Corporations on the Petroleum Industry, part I, p. 48. Referred to hereafter as Report on the Petroleum Industry.

[2] Report on the Petroleum Industry, part I, p. 48.

[3] Report of Hepburn Committee (New York), pp. 2615, 2695.

was the railroad rebate."[1] It is true that the progress of the industry in the seventies necessitated production on a considerable scale, and that the refiners who were not able to expand their operations were doomed in the competitive struggle. But the economies of large-scale production were secured by a considerable number of refiners, and hence the ability to produce on a large scale does not explain the growing preëminence of the Standard Oil Company—and especially since advantages in freight rates easily more than offset unusual economies in production.

The real struggle in the seventies, therefore, was to secure special railroad rates. And the railroad situation was such that the opportunities in this direction were exceptional. There had been rate wars between the Pennsylvania Railroad and the New York Central Railroad as early as 1869, the year in which both of these roads secured connection with Chicago. With the entrance into Chicago during the seventies of other railroads—notably the Baltimore and Ohio and the Grand Trunk—competition among the railroads for traffic became still more intense. The Standard Oil Company, as it happened, was well situated to demand special rates on its oil traffic. Its refineries at Cleveland were served by two railroads to New York City—the New York Central and the Erie—and also had water communication to the East by way of the Great Lakes and the Erie Canal. If railroad rates were unsatisfactory, there was this alternative water route. The railroads thus found themselves compelled to grant greater and greater concessions to the refiners at Cleveland, and the Standard Oil Company being the largest refining concern naturally received at least its share. But the Standard Oil Company was ambitious, apparently, to secure a still larger share; and through the South Improvement Company scheme was successful in effecting this end.

The South Improvement Company was a Pennsylvania corporation organized in January, 1872, under a charter granted in 1870, conferring almost unlimited powers.[2] The South

[1] Report on the Petroleum Industry, part I, p. 22.

[2] Ibid., p. 55.

Improvement Company, which was backed mainly by certain refiners in Cleveland and Pittsburg, was controlled by the Standard Oil group. The function of this company was to negotiate with the railroads for special rates in return for the privilege of carrying the large amount of traffic at the disposal of the company—rates much lower than were to be given to refiners not included in the South Improvement Company organization. In this plan the company was highly successful. It entered into contracts with the Pennsylvania Railroad, the New York Central, and the Erie, whereby its oil traffic was to be divided among these three railroads in certain proportions.[1] These contracts specified the rates on oil from the oil fields to the refining centers and to the seaboard, and expressly provided for rebates from these gross rates on all oil transported for the South Improvement Company. They further provided that similar rebates should be given to the South Improvement Company on all oil carried for other parties. As is brought out in a table in the report of the Commissioner of Corporations, the rebates ranged from about 40 to 50 per cent of the gross rates in the case of crude oil, and from about 25 to 45 per cent in the case of refined oil.[2] Moreover, the contracts had other objectionable features. They established very much higher gross rates on refined oil from points in the oil regions than applied from Cleveland and Pittsburg, where the leading concerns in the South Improvement Company were located (the rates from the oil region should have been at least as low, and perhaps lower than those from either Cleveland and Pittsburg); and they provided that the South Improvement Company should be supplied with duplicate copies of the waybills of all oil shipments, these waybills to show the name of the consignor, the place of shipment, the exact kind and quantity of product shipped, the name of the consignee, and the destination of the shipments. The South Improvement Company, as the Commissioner of Corporations pointed out, was thus to be provided with

[1] A copy of the contract entered into with the Pennsylvania Railroad is in House Report no. 3112, 50th Cong., 1st Sess., vol. 9, pp. 357–361.

[2] Report on the Petroleum Industry, part I, p. 56.

complete facilities for espionage upon the shipments of its competitors.

The South Improvement Company with its favorable contracts thus became a powerful club, which might be used by the Standard Oil Company in the fight against its competitors. The government in its suit against the Standard Oil Company charged that it was clearly the intention of the South Improvement Company to use these contracts to force into the Standard Oil Company such refineries as were wanted, and to crush out the balance.[1] This certainly to a considerable degree was the outcome. Within three months practically the entire independent oil business of Cleveland succumbed. At least twenty of the twenty-five independent refineries sold out to the Standard. As a result the capacity of the Standard Oil Company increased from about 1,500 barrels of crude oil a day to 10,000 barrels a day.[2] The Standard Oil Company upon the completion of this transaction had a capacity greater than that of all the refiners in the oil creek regions put together, and greater also than that of all the New York refiners. Whereas in 1870 it had refined about 10 per cent of all the oil in the country, it now refined over 20 per cent.

The South Improvement Company contracts, signed on January 18, 1872, went into effect on February 26.[3] Naturally they aroused the most bitter antagonism on the part of the independent oil interests. A mass meeting was promptly held at Titusville, Pennsylvania, and an organization to fight the South Improvement Company was formed. An embargo was at once imposed on the sale of oil to the South Improvement Company, and committees were sent to the legislature of Pennsylvania and to Congress to enter protest.

This agitation produced the desired effect. On March 25, 1872, the railroads signed a contract with the independents that all shipping of oil should hereafter be made on "a basis of perfect equality to all shippers, producers, and refiners, and that no

[1] Brief for the United States (no. 725), vol. I, p. 12.

[2] Tarbell, The History of the Standard Oil Company, vol. I, pp. 67–68.

[3] Montague, Rise and Progress of the Standard Oil Company, p. 28.

rebates, drawbacks, or other arrangements of any character shall be made or allowed that will give any party the slightest difference in rates or discrimination of any character whatever."[1] On March 28 the railroads officially annulled their contracts with the South Improvement Company, and put into force a new schedule of rates ranging about 40 per cent lower than those stipulated in the contracts. And on April 6, 1872, the legislature of Pennsylvania deprived the South Improvement Company of its charter.

Yet the Standard Oil Company continued to receive special rates. In 1879 Mr. H. M. Flagler, Mr. Rockefeller's partner, produced, before an Ohio Legislative Committee, contracts showing that from the first of April, 1872, to the middle of November, 1872, the Standard Oil Company had an east-bound rate on the NewYork Central of $1.25 per barrel of refined oil. This was 25 cents less than that provided for in the agreement of March 25, 1872, between the railroads and the independents.[2] Other instances of rebates in the seventies are cited in the report of the Commissioner of Corporations.[3] According to the Commissioner, at almost every turn rates were adjusted or manipulated in favor of the Standard Oil Company, and these favors were shown the company at a time when they were of peculiar value—that is, when it was endeavoring to establish its supremacy in the oil industry.[4] During this early period rebates were given to independent shippers also, but the concessions obtained by the Standard Oil interests were much greater than those obtained by their competitors.

Having acquired the refineries in its own district (Cleveland), the Standard Oil Company proceeded to extend the sphere of its influence. In 1874 it gathered in the important refineries of Warden, Frew and Company of Philadelphia, Charles Lockhart of Pittsburg, and Charles Pratt and Company of New York.

[1] House Report no. 3112, 50th Cong., 1st Sess., vol. 9, p. 361.

[2] Tarbell, The History of the Standard Oil Company, vol. I, p. 100. See also pp. 93–94.

[3] Report on the Petroleum Industry, part I, pp. 58 ff.

[4] Ibid., p. 66.

The subsequent acquisitions of the Standard Oil Company were promoted by the organization in 1874 of an "alliance" known as the Central Association of Refiners, Mr. John D. Rockefeller being its president. This association, which reminds one in some respects of the South Improvement Company, included a large percentage of the refining capacity of the country. The association agreement provided that the members were to operate their own refineries, but that the Standard Oil Company was empowered to determine the quantity of their output, to buy all their crude oil and to sell all their refined oil, and to negotiate with the railroads and pipe-lines as to freight rates.[1] It was thus a pool, and one that was able to bring great pressure to bear on the carriers. The formation of this association was followed by the rapid decline of the independent element. Within three or four years practically all of the independent refiners in the oil regions of northwestern Pennsylvania had either gone out of business or had sold to the Standard party.[2] Simultaneously, the independent group in the Pittsburg district was being rapidly absorbed; between 1875 and 1877 some twenty independent plants were acquired by Standard Oil interests. By 1877, moreover, practically the entire group of independent refiners in Baltimore had succumbed. As the result of these acquisitions, made possible in many cases by pressure, the Standard Oil Company and allied interests had secured by 1879, as noted above, from 90 to 95 per cent of the refining capacity of the country.

The Standard Oil Company was greatly aided in this enlargement of its business by its control of pipe-lines for transporting crude oil from the oil wells to the railroads. The building of local pipe-lines in the oil fields was begun in 1865. The Standard Oil Company did not originate pipe-line transportation, nor did it build any of the lines laid down in the first eight years.[3] But quite early its guiding spirits realized the importance of getting control of the pipe-lines. The entrance of the Standard

[1] Report on the Petroleum Industry, part I, pp. 49–50.

[2] Ibid., p. 50.

[3] Brief for the United States (no. 725), vol. I, pp. 45–46.

Oil group into the pipe-line business came in 1873. In that year J. A. Bostwick & Company—Mr. Bostwick was affiliated with the Standard Oil Company—built a local pipe-line in northwestern Pennsylvania. This concern later became the American Transfer Company, and as such was definitely a part of the Standard organization. In 1874 Standard Oil interests secured one-third of the stock of the United Pipe Lines, a company credited with 30 per cent of the pipe-line business of the Pennsylvania oil fields region. The United Pipe Lines with its new affiliations was able to secure favors from the railroads. It entered into an agreement with the New York Central and the Erie, by which it was to apportion to each road 50 per cent of its traffic, and in return was to receive a rebate of 10 per cent on all its shipments.[1] The other pipe-line systems likewise arrayed themselves with some railroad. The Empire Transportation Company allied itself with the Pennsylvania Railroad, and began the construction of oil refineries. The Standard Oil Company, not welcoming competition, and particularly when backed by railroad support, demanded, but without success, that the Empire Transportation Company give up its refineries. At the suggestion of the New York Central and the Erie, which would have been injured by the resulting diversion of oil traffic to the Pennsylvania, the Standard Oil Company in March, 1877, ceased shipping freight over the Pennsylvania. This precipitated a struggle, which lasted for six months. In one instance the Pennsylvania transported oil at a rate that was 8 cents per barrel below cost,[2] and the Empire Transportation Company sold oil in the territory of the Standard "alliance" at very low prices. But the Standard Oil Company with its allied railroads proved the stronger. In October, 1877, the Pennsylvania Railroad abandoned the struggle, and sold the Empire Transportation Company to the Standard Oil Company. The Pennsylvania Railroad and the Standard Oil Company then entered into a contract whereby the Standard was to divide its traffic among the Pennsylvania, the New York Central, the Erie, and the Baltimore and Ohio,

[1] Report of Hepburn Committee (New York), pp. 175, 182.

[2] House Report no. 3112, 50th Cong., 1st Sess., vol. 9, p. 176.

and in return was to receive a rebate of 10 per cent on all freight after May 1, 1878 (when the contracts of the Pennsylvania with its shippers were to expire).[1]

In the same year (1877) the Standard Oil Company acquired the Columbia Conduit Company, the only important independent pipe-line remaining in the oil regions. By the close of the year, therefore, the Standard Oil interests had obtained control, through stock ownership, of substantially all the pipe-lines in the oil region.[2] Hardly a barrel of oil could be brought to the railroads without the consent of the Standard organization. Mr. Rockefeller had begun with an ambition to be the only oil refiner in the country, but he had found it necessary in carrying out this purpose to secure control of the pipe-line system. The result, incidentally, was the acquisition of great power over the railroads,—power which was to assist in the maintenance of the monopoly which he had succeeded in building up.

The independents, however, died hard. To free themselves from the dominance of the Standard Oil Company, they organized in November, 1878, the Tide Water Pipe Company to construct a pipe-line from the oil fields of northwestern Pennsylvania to the seaboard, a distance of 109 miles.[3] The oil was to be pumped over the Alleghany Mountains. Up to this time oil had never been pumped more than 30 miles, and no considerable elevation had been overcome. The project was deemed quite impracticable both by the Standard Oil Company and by the railroads. Nevertheless, success crowned the venture. In June, 1879, oil flowed over the mountains, and into the receiving tank located on the eastern side. A new era in the oil business seemed to be at hand. Clearly it was but a matter of time before the Tide Water Pipe Company would pump oil into New York City, where there were a number of refiners anxious to free themselves of their dependence on the Standard Oil Company and the railroads. To meet this situation the Standard Oil Company acted

[1] Montague, The Rise and Progress of the Standard Oil Company, pp. 56–59.

[2] Brief for the United States (no. 725), vol. I, p. 46.

[3] Tarbell, The History of the Standard Oil Company, vol. II, p. 4.

with its usual dispatch and skill. The local pipeage rate was reduced by the Standard pipe-lines; and the through rate on crude oil was reduced by the railroads, in order to prevent this traffic from being lost to them,—the traffic would no longer bear the former rate. The railroad rate from the oil fields to New York Harbor, for example, was reduced from $1.15 per barrel to 30 cents.[1] The Standard Oil Company was given an even lower rate—20 cents—but in spite of this discrimination in its favor it remained at a disadvantage. According to an estimate of the engineer who built the independent pipe-line, oil could be piped to seaboard for 16 2/3 cents per barrel.[2] Apparently the day of the railroad as a long distance transporter of crude oil was past.

The Standard Oil interests, however, did not delay action until the outcome of the struggle between the railroads and the long distance pipe-line was known. Hardly had the new line proven a success, when the Standard interests began to build pipe-lines from the oil fields to Bayonne, New Jersey, to Philadelphia, and to the inland refining points at Pittsburg, Cleveland, and Buffalo. To carry on this vast program—destined to make the Standard Oil Company independent of the railroads with respect to the transportation of crude oil—the National Transit Company was incorporated in April, 1881, with a capital of $5,000,000.[3]

Meanwhile, the Standard Oil Company acquired most of the independent refineries about New York Harbor which the Tide Water Pipe Company proposed to feed.[4] To protect themselves, the supporters of the Tide Water Pipe Company at once began to build several refineries on the seaboard, the oil being stored pending their completion. Subsequently the Standard Oil Com-

[1] Report of the Commissioner of Corporations on the Transportation of Petroleum, p. 86. Referred to hereafter as Report on the Transportation of Petroleum.

[2] Tarbell, The History of the Standard Oil Company, vol. II, p. 11.

[3] Report on the Petroleum Industry, part I, p. 53. The United Pipe Lines, a system of local gathering lines, was transferred to the National Transit Company—the trunk line system—in 1884.

[4] Report on the Petroleum Industry, part I, p. 53.

pany contrived to acquire a minority of the company's stock.[1] This action, together with the determined opposition of the railroads, led to a practical surrender on the part of the Tide Water concern, and an agreement was reached in October, 1883, by which the Tide Water Company became for all practical purposes a part of the Standard Oil System.[2] The Standard Oil Company and its ally now collected practically all the crude oil produced, and independent enterprise was once more effectually discouraged.

By 1879, as we have seen, the Standard Oil Company had attained a position of supremacy in the refining industry. In that year, as explained in chapter III, the first "trust agreement" was entered into, an agreement which was revised and elaborated in 1882. Ten years later (in 1892) this agreement was declared illegal by the Ohio courts. For several years thereafter a community of interest arrangement was relied upon. But this arrangement was likewise attacked in the Ohio courts as not representing an honest attempt to comply with the order of the court, and hence in 1899 a decision was made to reorganize in New Jersey as a holding company.

Among the twenty principal companies comprising the Standard Oil organization was the Standard Oil Company of New Jersey, with a capital of $10,000,000. The charter of this company was now amended, and power obtained to engage in all kinds of mining, manufacturing, and trading, and to hold stocks and bonds. On June 14, 1899, the capital stock of the Standard Oil Company of New Jersey was increased to $110,000,000 through the issuance of $100,000,000 of common stock, the existing $10,000,000 being changed into preferred stock.[3] The New Jersey concern proceeded to exchange its stock for the stocks of the concerns which had formerly been controlled by the trustees,[4] but which now, upon the tardy liquidation of the trust certifi-

[1] Report on the Petroleum Industry, part I, p. 54.

[2] Ibid.

[3] Ibid., p. 84.

[4] A list of the companies controlled by the Standard Oil Company of New Jersey is in Report on the Petroleum Industry, part I, pp. 85 seq.

cates, were in the hands of the former holders of the trust certificates. Through this process of exchange the Standard Oil Company of New Jersey within a short period of time had outstanding all told about $97,250,000 of stock; and this was practically the amount of "trust certificates" issued and outstanding at the time of the dissolution in 1892.[1] The $10,000,000 of preferred stock of the Standard Oil Company of New Jersey—this preferred stock represented the total capital stock of the Standard Oil Company prior to the increase above noted—was given the same privileges of exchange as applied to the stocks of the other nineteen constituent companies, and it was readily exchanged for common stock in the Standard Oil Company of New Jersey, since under this company's amended charter dividends on the preferred stock were limited to 6 per cent, whereas it was practically certain that the common stock would receive much higher dividends. The preferred stock, after this exchange, was cancelled.

This reorganization, however, was one in form only. The Standard Oil Company of New Jersey (a holding company) became the owner of the stocks previously held by the trustees; the trustees (liquidating) were made directors of the holding company; and the holding company itself was controlled by the same individuals who had formerly held a controlling interest in the old trust certificates.[2] The trust had simply hung out a new sign.

The Standard Oil Company of New Jersey was thus principally a holding company. But it also refined and marketed oil on its own account. It owned the large refineries at Bayonne and Constable Hook, New Jersey, and it operated the Standard refineries at Baltimore, Maryland, and at Parkersburg, West Virginia. The refineries directly operated by the Standard Oil

[1] Report on the Petroleum Industry, part I, p. 84. There was no watered stock issued as the result of the reorganization of 1899. What water there was, if any, resulted from the issuance of the trust certificates in 1882.

[2] Mr. Rockefeller himself held 26.4 per cent of the stock of the Standard Oil Company of New Jersey. Report on the Petroleum Industry, part I, p. 95.

Company of New Jersey produced in 1904 approximately one-third of all the illuminating oil produced by the Standard organization.

The history of the Standard Oil Company and the forms of organization adopted by it have been briefly outlined. It is now proposed to consider in more detail the position attained by the Standard Oil Company, and the principal factors in its success. The treatment will deal in the main with the period from 1904 to 1906, the years which served as the basis for the reports of the Commissioner of Corporations.

In 1904 illuminating oil, or kerosene, was the most important product derived from crude oil, both in quantity and value. According to the United States Census the total production of refined oil [1] in 1904 was 27,135,094 barrels, or 1,356,754,700 gallons. Of this amount the Standard Oil Company produced at plants controlled directly by it, 21,341,179 barrels, or 78.65 per cent of the total.[2] The other refineries affiliated with it produced about 2,143,100 barrels, which, added to the Standard Oil output of 21,341,179 barrels, made a total of 23,484,279 barrels, or 86.55 per cent of the country's output.[3] This left 3,650,805 barrels as the output of the remaining concerns, or 13.45 per cent of the total. But not all of this remainder could properly be considered as independent. Some of the so-called independent refiners were unable to obtain crude oil except from the Standard itself. The Standard, of course, allowed them only as much crude oil as it chose, and in this way was able to prevent them from extending their business, and from becoming really effective competitors. It appears that of the total of about 3,650,000 barrels of refined oil produced by the companies not affiliated with the Standard Oil Company, some 1,160,000, or nearly one-third, were produced in refineries dependent for

[1] In customary usage the term "refined oil" refers to illuminating oil only, and it is so used in the Report of the Commissioner of Corporations.

[2] Report on the Petroleum Industry, part I, p. 265.

[3] Brief for the United States (no. 725), vol. I, p. 144, places the percentage at 87.30, and states that an employee of the Standard Oil Company verified the correctness of the computation.

their crude oil mainly or entirely on the Standard companies.[1] While these 1,160,000 barrels might not properly be treated as controlled by the Standard, neither could they be denominated really independent, in view of the conditions under which these companies secured their crude oil. If we deduct these 1,160,000 barrels, there would be left as independent approximately 2,500,000 barrels, or only a little over 9 per cent of the total production.

The effectiveness of the competition of the independents was even less than these figures would indicate, since their total production was distributed among a large number of concerns. In 1904 there were some seventy-five independent refiners all told.[2] The total output of these companies was less than that of either the Bayonne or the Philadelphia works of the Standard Oil Company. Had the total independent output been concentrated in a few large refineries, competition with the Standard Oil Company would have been much more vigorous and successful.

The aforementioned statistics relate to the production of refined oil in the United States, not to the consumption within the United States. But they also fairly indicate the Standard's proportion of the sales in this country, in spite of the fact that some 55 per cent of the country's output was then exported, because the Standard Oil Company's proportion of the export business was only a little greater than its proportion of the domestic production. According to the report of the Bureau of Corporations the Standard's proportion of domestic sales in 1904 was in the neighborhood of 85 per cent.[3]

Next in importance to illuminating oil among the products of crude petroleum were the naphthas (gasoline and benzine) and the lubricating oils. But no statistics were available showing the quantity of these products refined by the Standard Oil Company. The Commissioner concluded, however, that because of the physical limitations on varying the proportion

[1] Report on the Petroleum Industry, part I, p. 281.

[2] Ibid.,pp. 271–273.

[3] Ibid., p. 284.

of the different refined products derived from crude oil, it was safe to say that the Standard controlled in 1904 at least four-fifths of the country's output of naphtha and lubricating oil.[1]

That the Standard Oil Company possessed monopolistic power is evident. What were the chief sources of that power? The ability of the Standard to maintain a monopolistic position was not the result of the exclusive ownership of a limited natural resource; the Standard had no monopoly of the *production* of crude oil, the raw material. Though the company produced large quantities of crude oil, it produced but a small proportion of its own requirements. The total production of crude oil in the United States in 1905 was approximately 135 million barrels, and of this amount not over one-sixth was the product of wells owned by the Standard Oil Company or affiliated concerns.[2] Its interest in crude oil production seems to have been greatest in the Pennsylvania and Lima oil fields. In 1906 Standard Oil interests produced 26 per cent of the crude oil output of the Pennsylvania field, and 31 per cent of the output of the Lima field.[3] In other fields, however, such as the Mid-Continent, California, Colorado, and Gulf, its production was quite small.[4]

There were at least two reasons why the Standard Oil Company did not attempt to monopolize the refining industry by means of the ownership of the supply of raw material. In the first place, the Standard probably obtained its oil cheaper by buying a large part of it than it could have obtained it by producing the entire supply itself. The highly speculative character of the oil business, like gold mining, probably caused crude oil to be sold on the average for less than the cost of production, at least during considerable periods of time. The Standard therefore allowed others to take the risks of prospecting, and of opening

[1] Report of the Commissioner of Corporations, part I, p. 282. In the brief for the government it was charged that the Standard with its affiliated companies manufactured in 1904, 82.9 per cent of the naphtha produced in the United States. Brief for the United States (no. 725), vol. I, p. 144.

[2] Report on the Petroleum Industry, part I, p. 8.

[3] Brief for the United States (no. 725), vol. I, p. 139.

[4] Report on the Petroleum Industry, part I, pp. 118–119.

up new fields, and confined its efforts in the line of crude oil production to the better developed areas. Secondly, and probably more important, the Standard was able to secure control of the crude oil supply without producing it itself. The ownership by the Standard of the pipe-lines, the only effective means of marketing most of the oil, gave it just as complete control of the supply of crude oil as if it had held title to the oil fields. Because of its control of the pipe-lines, the Standard in many districts was almost the sole purchaser of crude oil, and this practically enabled it to fix the price. In the Pennsylvania, Lima-Indiana, and Mid-Continent fields—the principal fields producing oil suitable for refining—the Standard Oil Company daily published the price that it would pay for crude oil, and this price was the public market price. Prior to 1895 oil had been bought and sold at oil exchanges located in New York, Pittsburg, and Oil City, Pennsylvania. But these exchanges were discontinued in 1895 on account of an announcement by the Standard that it would no longer purchase oil on the basis of the prices established on the exchanges; and thereafter the Standard itself named the price.[1]

It has been urged on behalf of the Standard Oil Company that its monopoly power was due to the great ability of its managers, and the consequent efficiency of its plants and organization. That the company all through its history has been highly efficient is questioned by no one. And yet the Standard Oil Company has had no monopoly of business ability; it has been ability of the same high order that developed our railroads, our mineral resources, our timber lands, and our industries generally. The "captain of industry" has been conspicuous in all lines of business. The Standard Oil officials may have been "smarter" than their fellows, as Mr. W. H. Vanderbilt once said, but, as will be pointed out later, it was not their ability alone that enabled the Standard to develop and maintain its monopoly.

But if the Standard's monopoly power may not be ascribed primarily to the efficiency of its managers, may it not be the

[1] Brief for the United States (no. 725), vol. I, p. 165.

result of the economies of the trust form of organization? Did the establishment of a trust make it possible for the Standard to produce more cheaply than its competitors, combined though some of them were, and was the Standard able to retain its monopoly by the practice of maintaining such a low level of prices the country over that competition was impossible? This is a matter that deserves more detailed analysis than has yet been given to it by any governmental investigating body, even including the Bureau of Corporations. Needless to say, it is not within the power of the individual investigator to secure the desired data. However, we are not altogether in the dark upon the question at issue, since the Bureau did make quite an extended investigation into the relative costs of refining at the Standard and at the independent plants.

Whatever superiority the Standard Oil Company possessed over the independents in the refining business must be attributed, said the Bureau, chiefly to one of two causes: (1) the possession of a considerable number of plants; (2) the large size of its plants.

(1) The Standard Oil Company with plants scattered all over the country was able to reduce transportation charges, i. e., to eliminate cross freights. It could supply each section of the country from its nearest plant, and thus effect a saving as compared with the refiner who had to distribute from a single refinery.[1] The Standard Oil Company in 1906 owned or controlled the output of over twenty refineries located in twelve states, scattered from New York Harbor to San Francisco Bay, and from the Great Lakes to the Gulf of Mexico. No independent refiner, however, had more than three refineries, and only two or three had more than one.[2] The Standard refineries, moreover, were as a rule much nearer the large consuming centers.

The possession of a number of refineries doubtless conferred an additional advantage through the possibility which thus arose of comparing the results at different plants, and of carrying on experiments in individual plants without involving the

[1] From this it follows, of course, that the refiner with a single plant had only a limited market.

[2] Report on the Transportation of Petroleum, p. 29.

entire volume of business. There may also have been the possibility of reducing the cost of general administration and of superintendence. However, the economies directly attributable to the possession of numerous refineries, aside from the saving in cost of transportation, were, in the opinion of the Commissioner of Corporations, by no means great.[1]

(2) The Standard also had an advantage over the independents because of the large size of its individual plants. In the eighteen plants directly controlled by it the Standard produced, in 1904, 21,341,000 barrels of illuminating oil, while the 75 or more independent plants in the country had an output of only about 3,650,000 barrels. The Standard plants at Bayonne and at Philadelphia each produced approximately 5,000,000 barrels, or about 50 per cent more than all the independent plants put together. The largest independent concern in 1904 produced only about 200,000 barrels of illuminating oil. After 1904 several independent concerns enlarged their refineries, or constructed new ones which approximated the average size of the Standard plants, yet none of the independent plants could compare in size with the largest Standard plants.

The superiority of the large Standard plants, however, was by no means as pronounced, said the Bureau of Corporations, as the representatives of the company claimed. This superiority would be expected to manifest itself in two different ways—first, in a lower cost per unit of product; and, second, in better yields, i. e., a less amount of waste and larger proportions of the more valuable products. With regard to the first point, the Bureau declared that there was no great difference in refining costs as between the plants of the independents and the plants of the Standard. Data gathered by the Bureau from nine independent refineries (the only ones whose costs were closely comparable with those of the Standard refineries) showed operating costs of refining ranging from 24.91 cents per barrel of crude to 35.53 cents, and averaging 29.28 cents.[2] Data regarding the Standard Oil Company's refining costs were collected for the following six

[1] Report on the Petroleum Industry, part II, p. 650.

[2] Ibid., p. 653.

plants: Sugar Creek, Missouri, and Neodesha, Kansas (combined), 15.46 cents per barrel; Chaison, Texas (Security Oil Company, an affiliated concern), 27.0 cents; Lima, Ohio, 29.29 cents; Richmond, California, 32.8 cents; Florence, Colorado (United Oil Company, which sells its whole output to the Standard), 33.6 cents.[1] From an examination of the costs at these six plants it appears that, with the exception of the Sugar Creek and Neodesha refineries, the operating expenses of the Standard plants were approximately the same as those of the independents for which data were available; and the Sugar Creek and Neodesha plants may not properly be compared with these independent plants, since they did not elaborate by-products.[2] The Lima plant of the Standard was found to be most nearly comparable to the independent plants whose costs had been secured, since it carried the elaboration of by-products to practically the same degree of completeness. The operating costs of the Lima plant were, in fact, almost exactly the same as the average for the nine independent plants—29.29 cents as compared with 29.28 cents. It is possible, said the Bureau, that some of the larger Standard refineries had slightly lower costs, but in any event the difference between the average operating cost for all the Standard refineries and for the more efficient independent refineries did not, at the most, exceed one-eighth of a cent per gallon.[3]

With respect to the yield of products, satisfactory statistical data were not available. It was known that some of the Standard plants elaborated their by-products more fully than any independent plant, and also that the Standard plants on the whole secured more of the high grade by-products. But it is not probable, the Commissioner maintained, that there was a very great difference in efficiency with respect to yields as between the best Standard plants and the best independent plants.[4]

[1] Report on the Petroleum Industry, part II, pp. 653–654. The Bureau did not secure any direct information as to the costs of production at the Standard's plant in Whiting.

[2] Report on the Petroleum Industry, part II, p. 654.

[3] Ibid., p. 655.

[4] Ibid., p. 651.

Taking into account both the cost of refining per unit and the yield, it is probably safe to say, stated the Commissioner, that the advantage of the Standard over the independent plants was not more than one-fourth of a cent per gallon in the cost of finished products, and at the outside it would not exceed one-half of a cent per gallon.[1]

To what was this advantage of the Standard due? Did it represent the economies of the trust form of organization, or did it result from the fact that the largest plants were owned by the trust? To put it differently, was the Standard's low refining cost the result of combination or of large-scale production? Upon this point the report of the Bureau returned no conclusive answer, since the costs at the large Standard plants were not shown.

It is clear from what has been said that the Standard, in part because of the volume of its business, and the consequent greater size of its plants, did refine somewhat more cheaply than its competitors.[2] Yet the Standard would have effected a monopoly through low production costs only if it had been willing to charge prices generally so low that the independents could not produce at a profit. But this was not its policy. The Standard, to be sure, did cut prices in certain localities to make it uncomfortable for its competitors, but this is quite different from a policy of low prices generally—a policy that would have cut in severely on the Standard's profits. And the fact that the Standard was able to maintain its control of the industry while at the same time charging prices so high that many of the independents made ample profits, in spite of the difficulties under which they labored, must mean that the Standard resorted to other methods of restraining competition. Beyond question, says the Commissioner of Corporations, the dominant position of the Standard Oil Company in the refining industry was due to unfair practices—to abuse of the control of pipe-lines, to railroad discriminations, and to unfair methods of competition

[1] Report on the Petroleum Industry, part II, p. 655.

[2] The Standard had a further advantage over its competitors through the ownership of pipe-lines, but, as will be shown later, this did not constitute a legitimate advantage.

in the sale of the refined petroleum products.[1] These practices will therefore be considered in some detail.

Throughout its entire history the foundation of the Standard Oil Company's success has been the element of transportation. The advantages in transportation possessed by the Standard have been two-fold: those resulting from its ownership of pipe-lines for transporting crude oil; and those resulting from railroad discriminations in the transportation of the refined products of crude oil.

Ownership of Pipe-Lines

Most of the crude oil produced in this country, with the exception of that produced in California, Texas, and Louisiana, is refined before being consumed.[2] It reaches the refineries mainly by means of pipe-lines. A net work of small pipes gathers the oil from the wells, and except where the refinery is quite near to the wells, the oil is conveyed to the refining point by means of trunk lines, often of great length. The process by which the Standard interests acquired a practical monopoly of the pipe-line system has already been described. This monopoly it was able to maintain. In 1904 the Standard controlled 88.7 per cent of the pipe-line business of the Pennsylvania field, and 93.5 per cent of that of the Lima-Indiana field.[3] There were apparently no competing lines whatever in the Illinois field, and up to 1906 there was substantially no competition in the Mid-Continent field.[4]

The methods employed by the Standard to maintain its monopoly of the pipe-line business were thoroughly investigated by the Bureau of Corporations. The conclusions of the Bureau were substantially as follows:[5]

(1) The Standard interfered with the construction of inde-

[1] Report on the Petroleum Industry, part I, pp. 276–277.

[2] The oil of these states is not so suitable for refining, and is used largely for fuel in its natural condition.

[3] Brief for the United States (no. 725), vol. I, pp. 140–141.

[4] Ibid., pp. 141–142.

[5] Report on the Petroleum Industry, part I, pp. 153–154.

pendent pipe-lines in various ways. Having once constructed its own line, it used its influence to prevent the passage of laws giving pipe-lines the right of eminent domain. In the absence of such laws, and to some extent even when they existed, it was able to hinder or prevent the construction of independent pipe-lines by buying up or securing control of lands over which they had to pass, and by influencing railroads to refuse pipe-lines the right to cross their tracks. (2) When the Standard was unable to prevent the construction of independent pipe-lines it sought to control them by acquiring their stock. (3) The Standard at times induced crude oil producers who were relied upon to furnish oil to independent pipe-lines, or refiners who were relied upon to take the oil, to refrain from doing so. This policy was frequently accompanied by outright purchase of the crude-oil properties or refineries. By this means the volume of business of the independent lines was restricted, and the cost of pipeage proportionally increased. (4) The Standard by the payment of premiums for crude oil produced in the territory reached by the independent pipe-lines made it difficult for independent pipe companies to obtain oil for transportation over their lines. Most of the independent pipe companies, like the Standard itself, purchased practically all the crude oil which they handled. The payment of a premium meant that a higher price was offered for the crude of a particular area than was offered for crude elsewhere in this same field. By paying a premium the Standard was able to prevent the independent pipe-lines from getting an adequate supply of oil, or else to force them also to pay premiums, with a consequent diminution in their profits. Since the independent pipe-lines were all comparatively small concerns, reaching only a limited area, the Standard by paying these premiums in certain localities greatly reduced their profits, while itself sustaining comparatively little loss on the entire volume of its business. The practice of paying premiums on crude oil is similar in principle and effect to the practice of selling refined products at a cut price in certain markets (local price discrimination). The payment of premiums was, on the whole, the most important of the unfair practices of the Stand-

ard in preventing the development of competition in the pipe-line business.

The practices above enumerated by the Commissioner resulted in legislation dealing with the situation. In 1906 pipe-lines were declared by the Hepburn Act to be common carriers. This made them subject to the provisions of the law requiring the charging of reasonable and non-discriminatory rates, and the filing of these rates with the Interstate Commerce Commission. The constitutionality of this law, however, was disputed, and meanwhile the pipe-line companies controlled by the Standard rendered the law practically inoperative, according to the Commissioner of Corporations, by their refusal to accept the obligations of common carriers.[1] The companies endeavored in various ways to prevent outside shippers from making an effective use of the Standard pipe-lines. We quote again substantially from the report of the Bureau.[2] (1) Some of the Standard pipe-lines filed no tariffs with the Commission, and refused to transport any oil for others. To avoid doing so they sought in some cases to confine their business, or at least pretended to confine it, within the boundaries of individual states. (2) Though some of the Standard's pipe-lines filed their rates with the Commission, the rates specified were almost identical with the rates of the railroads between these same points. The rates charged, furthermore, were much in excess of the cost of the service, and were thus unreasonable.[3] (3) The tariffs filed by those Standard pipe-lines that did comply with the law in this respect were more remarkable for their omissions than for the rates which they quoted. For example, no rates were given to New York Harbor, either in the state of New York or in the state of New Jersey, and no rates to Baltimore, Maryland. These were points to which outside shippers would very naturally wish to send oil. On the other hand, numerous rates were quoted to places

[1] Report on the Petroleum Industry, part I, p. 183.

[2] Ibid., pp. 183–191.

[3] Ibid., pp. 35–36. On the wide margin between pipe-line costs and rates, see also the Report of the Federal Trade Commission on Pipe-Line Transportation of Petroleum, pp. 18–20.

where no one would care to deliver oil. (4) Finally, even when the Standard pipe-lines did file tariffs indicating an apparent willingness to transport oil for others, they established regulations that virtually prevented shipments. Most of the tariffs filed by the Standard required shipment to be made in quantities of not less than 75,000 barrels, and in the case of some of the lines, 300,000 barrels, minima so high as virtually to prevent the use of the pipe-lines by outside shippers.

While such tactics as these did not indicate a disposition to comply with the requirements of the law, the Commissioner pointed out that possibly the action of the Standard pipe-line companies did not represent their finally determined policy. The act had just been passed, and the Interstate Commerce Commission had not yet made any regulations with respect to pipe-lines, or decided any cases involving their rates. But the report of the Federal Trade Commission on Pipe-Line Transportation of Petroleum makes it clear that obstructionary tactics were to be the Standard's determined policy;[1] that the law was not to be obeyed until its constitutionality had been decided by the Supreme Court. And this did not come to pass until 1914. Several years after the passage of the Hepburn Act in 1906, the Interstate Commerce Commission had issued an order requiring the Standard and other pipe-line companies to file with the Commission schedules of their charges for the transportation of oil.[2] The defendants brought suit in the Commerce Court to set aside the order, and that court issued a preliminary injunction, holding the statute to be unconstitutional.[3] But in 1914 in the Pipe-Line Cases the Supreme Court fully upheld the constitutionality of the law.[4] The interstate pipe-lines thereupon filed their rates with the Commission, but they had succeeded in staying the operation of the law, so far as they were concerned, for a period of eight years.

The excessive pipe-line rates charged the independent refiners were likewise charged the Standard refining companies. But this clearly was a matter of indifference to the Standard organi-

[1] See pp. 20–22.
[2] 24 I. C. C. Reports 1–11 (June 3, 1912).
[3] 204 Fed. Rep. 798.
[4] 234 U. S. 548.

zation. It was simply a question of where the profit of the organization as a whole was mainly to be made, whether in transportation or in refining. To the independent refiner, however, a high pipage rate was a vital matter. An unreasonable rate reduced correspondingly his total profits, and might cause him to do business at a loss. At times the rate on crude oil from the Appalachian field to the seaboard was more than 25 cents per barrel higher than the cost of transportation, including in that cost a profit of 10 per cent on the cost of reproducing the pipe-lines.[1] This was over half a cent per gallon, and half a cent would yield a profit of about 10 per cent on the investment required to carry on the refining business.[2] It is clear that the opportunities for competition in the refining of oil would have been much greater had the Standard pipe-lines been compelled to carry oil for others at a reasonable rate. In fact, not only the prosperity, but, according to the Federal Trade Commission, perhaps even the existence of many small concerns was dependent on lower pipe-line rates and reasonable minimum shipments.[3]

The control of the pipe-lines with the refusal to charge reasonable rates on the transportation of crude oil gave the Standard a further advantage over the independents, in that it was enabled to locate its refineries more advantageously than the independents. Thus, the Standard refineries were located for the most part near the centers of consumption, its two largest refineries being on the Atlantic seaboard, and its third largest being at Whiting, Indiana (near Chicago). It was the low cost of transporting crude oil by pipe-line that made it possible for the Standard Oil Company to locate its refineries so far from the oil wells. On the other hand, the high rates charged on oil transported through the pipe-lines forced the refiners not possessing pipe-lines to locate their refineries near the supply of raw material, and to distribute their refined products from such points. Thus, the main centers of independent oil refining in 1906 were in west-

[1] Report on the Petroleum Industry, part I, p. 38.

[2] Ibid.

[3] Report on Pipe-Line Transportation of Petroleum, p. XXXII.

ern and northwestern Pennsylvania, and northwestern Ohio. There were only four independent plants on the Atlantic coast, near to the populous cities of the seaboard and to the export markets; and none at Whiting, the distributing point for the western and southern markets.

The advantage in locating near the market obviously arose out of the fact that the cost of transporting crude oil in pipe-lines was much less than the cost of transporting the refined product to market by rail or water. Whereas the entire cost of transporting crude oil by pipe-line from the Appalachian field to the Atlantic seaboard did not exceed one-fourth of a cent per gallon, the freight rate on refined oil from the independent plants in western Pennsylvania to New York Harbor was about one cent per gallon.[1] Naturally the independent refiners preferred to locate their plants on the seaboard, rather than near the oil fields, yet this was not practicable, since, as has been stated, the Standard pipe-lines charged prohibitive rates for the transportation of crude oil, the pipeage rates to independent shippers being several times the actual cost of transportation to the Standard pipe-lines. The independents might still have located near the centers of consumption had the rail rates on the transportation of crude oil been comparatively low, but this was not the case. Generally speaking, the rail rates were as high or even higher than the pipe-line rates, high as these were.[2]

It might be asked why the independent refiners did not build pipe-lines of their own, if the location of their refineries near the markets was prevented by the excessive rates charged by the Standard pipe-lines. The explanation is that pipe-line transportation for long distances is economical only when the volume of traffic is large; and the unfair methods of the Standard had prevented the independents, with a few notable exceptions, from building up a business sufficient to justify the investment. The United States Pipe Line Company did succeed in constructing a trunk pipe-line, but because of the opposition of both the

[1] Report on the Transportation of Petroleum, p. 62.

[2] Report of the Federal Trade Commission on Pipe-Line Transportation of Petroleum, pp. 22–24.

Standard Oil Company and the railroads it took it nine years to complete its line to tidewater. An earlier enterprise—The Tide Water Pipe Company, the first company to lay a pipe-line to the seaboard—was so harried by the Standard interests that it eventually capitulated. Had the independents been left alone, they would undoubtedly have much extended their pipe-line facilities.

It is apparent that if there is to be effective competition in the sale of petroleum products, the pipe-lines, which carry the crude oil, must be open to all refiners on equal and fair terms, both as to rates and facilities. The analogy of the anthracite railroads and the commodity clause would suggest the desirability of definitely separating the ownership of the pipe-lines and of the refineries. Whenever a carrier has a financial interest in reducing the volume of traffic offered to it for transportation over its line, it is only with great difficulty, if at all, that it can be forced to offer satisfactory facilities at reasonable rates to its would-be patrons. The Federal Trade Commission, it may be observed, has strongly recommended that the ownership of the pipe-lines be segregated from the other branches of the petroleum industry.[1]

Railroad Discriminations

Through its ownership of pipe-lines the Standard had an advantage over its competitors. In addition, through railroad discrimination it was able to get its refined products to market on better terms than the independents.

In the petroleum business the cost of transportation is a vital factor. The importance of transportation arises out of the fact that the cost of refining, even including in the cost a reasonable profit to the refiner, is very low as compared with the freight rates on the transportation of refined oil to market. The operating expense of refining averaged in 1906 about three-fourths of a cent per gallon.[2] A net return of one-half a cent per gallon was considered an ample profit.[3] It follows, therefore, that one and

[1] Report on Price of Gasoline in 1915, pp. 17–18.

[2] Report on the Petroleum Industry, part II, p. 14.

[3] Report on the Transportation of Petroleum, p. 34.

a half cents per gallon provided abundantly for operating expenses and profit. But this was less than the freight rate on refined oil for transportation for any considerable distance. The rates from the oil regions of Pennsylvania and Ohio to the markets of the middle west ranged, roughly, from two cents to three cents per gallon.[1] It is apparent, therefore, that a comparatively slight difference in rates might enable one refiner to sell at a profit while his competitor was losing money. And in this industry, as in most all others, it is the relativity of rates, rather than the amount of the rates themselves, which most concerns the shipper.

Illustrations of railroad discrimination in favor of the Standard Oil Company during the early years of its history have already been given. The present account deals only with the advantages enjoyed by the Standard at the time when the Bureau of Corporations published its report on the Transportation of Petroleum. To quote from this report:

"The general result of the investigation [into transportation conditions for the preceding three or four years] has been to disclose the existence of numerous and flagrant discriminations by the railroads in behalf of the Standard Oil Company and its affiliated corporations. With comparatively few exceptions, mainly of other large concerns in California, the Standard has been the sole beneficiary of such discriminations. In almost every section of the country that company has been found to enjoy some unfair advantages over its competitors, and some of these discriminations affect enormous areas."[2]

The discriminations enjoyed by the Standard in the transportation of oil were classed in the report of the Bureau under four heads: (1) secret and semi-secret rates; (2) discriminations in the open arrangement of rates; (3) discriminations in classification and rules of shipment; (4) discriminations in the treatment of private tank cars. Data on the first two only will be here presented.

(1) Two leading instances of secret and semi-secret rates

[1] Report on the Transportation of Petroleum, p. 34.

[2] Ibid., p. 1.

may be cited.[1] The first deals with rates from Whiting, Indiana, into the South.[2] The published tariff from Whiting into the South was made up of a rate of eleven cents per hundred pounds to the Ohio river plus rates of varying amounts from the Ohio river south. This arrangement had long been in force, and was known to all shippers. The Standard Oil Company, however, shipped its oil into the South on an especially low rate applying to shipments between Dolton, Illinois, and Grand Junction, Tennessee. This rate would have been open to all shippers had they known of its existence; but they did not, since Dolton was an unimportant junction point near Chicago, and the ordinary shipper would never have thought of looking up the rate from Dolton. The Standard Oil Company knew of it, however, since it was made for its benefit. The secrecy of the Dolton rate is proven by the fact that the Chicago and Eastern Illinois, the road making the rate, reported to the Bureau rates from Whiting to the South much higher than those which were accorded to the Standard Oil Company on shipments by way of Grand Junction. By means of this secret combination of rates via Grand Junction the Standard shipped oil into a large part of the South at an average of one-fourth less than the published rate from Whiting, and approximately one-third less than the rates from competitive refining points in Ohio and Western Pennsylvania no farther distant. These discriminatory rates had hardly been uncovered by the Bureau before they were cancelled by the railroad. But meanwhile the business of the independents had been much damaged.

To cite a second instance,[3] the only published rate on oil between Whiting and East St. Louis, Illinois, was the regular class rate of 18 cents per 100 pounds. But the Standard, practically from the opening of its Whiting refinery in 1890, had been charged only 6 cents per 100 pounds. The shipments of the Standard Oil Company were very large, practically its entire

[1] For other instances, see Report on the Transportation of Petroleum, pp. 8 seq.

[2] Described in Report on the Transportation of Petroleum, pp. 6–7, 12.

[3] Ibid., pp. 12–14.

southwest business being handled from Whiting through East St. Louis. The independent refiners in northern Ohio and western Pennsylvania were charged from 17 to 24½ cents on shipments to East St. Louis, or from 11 to 18½ cents per 100 pounds more than the Standard rate to St. Louis from Whiting. Had the adjustment of rates on oil been on the same basis as on most other commodities, Whiting would have enjoyed lower rates to St. Louis than would centers of independent refining, but the difference in favor of Whiting would not have been more than five to ten cents, instead of eleven to eighteen and a half cents. With the aid of this six cent special rate, combined with other minor discriminations in the rates beyond East St. Louis, the Standard Oil Company was enabled to establish a well-nigh complete monopoly throughout the southwest. As soon as this secret six cent rate was uncovered by the Bureau—the railroad officials admitted it was secret—it was cancelled, and a rate of 10 cents per 100 pounds was substituted therefor. Yet even this 10 cent rate was unreasonably favorable to the Standard plant at Whiting as compared with rates from competing refining points to East St. Louis.

The secret rates enjoyed by the Standard Oil Company naturally helped it to maintain its monopolistic position. With the aid of its favorable freight rates, the Standard was able to sell oil in competitive areas at prices which were profitable to it, but which left no profit to its competitors. Upon the elimination of the competitors, the Standard advanced its prices to several cents above the cost of refining, and thus made enormous profits.

(2) Discriminations in the open arrangement of rates. Almost as important as the secret discriminations in rates were the open discriminations. To quote from the report of the Bureau:

"Almost everywhere the rates from the shipping points used exclusively, or almost exclusively, by the Standard are relatively lower than the rates from the shipping points of its competitors. Rates have been made low to let the Standard into markets, or they have been made high to keep its competitors out of markets. Trifling differences in distances are made an

excuse for large differences in rates favorable to the Standard Oil Company, while large differences in distances are ignored where they are against the Standard. Sometimes connecting roads prorate on oil—that is, make through rates which are lower than the combination of local rates; sometimes they refuse to prorate; but in either case the result of their policy is to favor the Standard Oil Company. Different methods are used in different places and under different conditions, but the net result is that from Maine to California the general arrangement of open rates on petroleum oil is such as to give the Standard an unreasonable advantage over its competitors.

The conclusion is unavoidable that the Standard Oil Company has had an important voice in the construction of such rates."[1]

As illustrating the favoritism shown the Standard Oil Company we refer again to the rates out of Whiting, Indiana.[2] The Whiting refinery was the Standard's most important refinery from the standpoint of distribution in this country; it produced one-third of all the refined oil sold by the Standard in the United States. Into practically all of the territory served by it, the open rates from Whiting were lower than the geographical location of the plant justified. This advantage was increased through the refusal of the railroads to prorate on oil. Prior to the opening of the Whiting refinery the western railroads had prorated on shipments of oil from the eastern refining points to the Middle and Far West, as they had on practically all other commodities. But shortly before 1890 the railroads discontinued this practice, so far as oil shipments were concerned. This meant that the eastern refiners, in order to get into western markets, had to pay the local rate to Chicago plus the rate from Chicago to destination. The disadvantage to which they were put in competition with the Standard plant at Whiting was thus measured by the local rate to Chicago, which amounted to from twelve to nineteen and a half cents per hundred pounds. Had prorating arrangements been maintained, this disadvantage would have been much less.

Notwithstanding the subsequent cancellation of the secret

[1] Report on the Transportation of Petroleum, pp. 20–21.

[2] Described in Report on the Transportation of Petroleum, pp. 21-22.

rates to Grand Junction and other points, Whiting was still favored over independent refining centers in the open rates into the entire south. From Whiting into the south the rate on oil was three and a half cents less than from Toledo, four cents less than from Cleveland, and seven and a half cents less than from Pittsburg, although on other commodities the rates from all these cities were practically the same as from Whiting. The success of this policy of discrimination between refining points was largely dependent, of course, upon the fact that a large proportion of the Standard's traffic originated at places where the independent refiners had no plants. The Standard supplied the greater part of the oil which it distributed in the United States from its great refineries at the seaboard and near Whiting, and there were few competitors at the seaboard and none at Whiting.

Unfair Methods of Competition in the Sale of the Refined Petroleum Products

The most important of the unfair practices of the Standard, so far as they relate to selling, has been local price cutting, or local price discrimination as it is generally called. The prices charged by the Standard Oil Company for petroleum products have varied greatly in different towns according to the amount of competition. This has been true of all petroleum products, but has been most glaring with respect to illuminating oil and gasoline. After making allowance for freight charges, which generally form a considerable part of gross prices, marked differences in prices appeared, not only between different states or sections of the country, but also between the different towns of each state. These differences in prices could sometimes be explained, in part at least, by differences in production and marketing costs, yet in many cases they reflected solely the intensity of competition encountered.

The fact of varying prices in different sections, indicating local price discrimination, is shown by the following table, giving the average price (less freight charges) paid by retailers for illuminating oil purchased from the Standard.[1]

[1] Report on the Petroleum Industry, part II, p. 31.

AVERAGE PRICE OF ILLUMINATING OIL,[1] LESS FREIGHT, DECEMBER, 1904, BY STATES

	Cents per gallon
North Atlantic Division:	
Maine	10.4
New Hampshire	10.3
Vermont	9.0
Massachusetts	9.9
Rhode Island	9.6
Connecticut	8.9
New York	10.0
New Jersey	9.8
Pennsylvania	8.7
South Atlantic Division:	
Delaware	7.7
Maryland & D. C.	9.2
Virginia	9.7
West Virginia	9.0
North Carolina	10.3
South Carolina	10.8
Georgia	11.6
Florida	12.8
North Central Division:	
Ohio	8.5
Indiana	9.3
Illinois	9.1
Michigan	9.0
Wisconsin	9.2
Minnesota	9.6
Iowa	10.2
Missouri	10.9
North Dakota	11.1
North Central Division (cont.):	
South Dakota	12.9
Nebraska	10.5
Kansas	11.4
South Central Division:	
Kentucky	9.4
Tennessee	11.6
Alabama	11.6
Mississippi	9.8
Louisiana	9.5
Arkansas	13.9
Indian Territory	12.5
Oklahoma	14.0
Texas	11.6
Western Division:	
Montana	15.6
Idaho	15.6
Wyoming	15.6
Colorado	16.2
New Mexico	13.2
Arizona	10.7
Utah	14.8
Nevada	16.4
Washington	15.7
Oregon	15.3
California	11.1
Northern California	12.4
Southern California	7.2

From this table it appears that the average price of illuminating oil was lowest in Delaware—7.7 cents per gallon—and highest in Colorado—16.2 cents per gallon—not counting Nevada, the quotation for which represented only one town. The average price in Colorado was thus more than twice the average

[1] There are several grades of illuminating oil, but most of the oil sold in this country is the second grade of water-white oil, and the prices of illuminating oil quoted in the Report of the Bureau of Corporations are for the most part the prices of this grade of oil.

price in Delaware. According to the Report of the Bureau of Corporations not more than three and one-half cents of the difference in price in these two states could be explained by differences in producing and marketing costs; and of course none of the difference in price could be explained by differences in freight rates, since the price in each case was that paid by the retailer, less freight charges from the Standard refinery.

Again, the prices (freight rates deducted) within the Mississippi basin from the Northern border to the Gulf of Mexico ranged from 8.5 cents in Ohio, where several independent plants were located, to 13.9 cents in parts of Arkansas. This territory was largely supplied with oil by the Standard refineries at Whiting, Indiana, and Cleveland and Lima, Ohio; and these refineries used the same kind of crude oil, and had practically the same production costs. In fact, most of this area was served by the Whiting refinery alone.

A very striking instance of sectional price variation is found on the Pacific coast. The Standard refined oil at its great refinery near San Francisco. The average price of this oil, the freight rate deducted, in December, 1904, was 7.2 cents per gallon in southern California, and 12.4 cents per gallon in northern California. The obvious explanation is that there were independent refineries in southern California. In Oregon, which drew its supplies from the same source, the price (freight rate deducted) averaged 15.3 cents per gallon, and in Washington, 15.7 cents. The price in the northern Pacific states was thus more than twice as high as in southern California for exactly the same oil.

The figures for gasoline show practically the same amount of price variation between the several states and sections of the country as has been shown to exist in the case of illuminating oil.

Equally significant are the differences in prices charged for illuminating oil and gasoline in towns within the same state. This subject is fully discussed in the report of the Bureau of Corporations, and the details need not be reproduced here.[1]

[1] See Report on the Petroleum Industry, part II, pp. 35–39, 480–507, 520–522.

Summarizing the data, in thirty-one of the states and territories, the range between the highest and lowest price of illuminating oil, freight deducted, was at least 3 cents; in ten states the range was at least 5 cents; and in one state—New Mexico—the highest price charged within the state exceeded by 13.2 cents per gallon the lowest price charged. In most cases, according to the report, only a small part of these differences in price within a single state was attributable to differences in marketing cost.

With respect to a number of the towns in which the price of illuminating oil was relatively low, the Bureau made inquiry into the cause thereof, and found that in the majority of cases these low prices were due to the existence of active competition. To quote from the report:

"The evidence is, in fact, absolutely conclusive that the Standard Oil Company charges altogether excessive prices where it meets no competition, and particularly where there is little likelihood of competitors entering the field, and that, on the other hand, where competition is active, it frequently cuts prices to a point which leaves even the Standard little or no profit, and which more often leaves no profit to the competitor, whose costs are ordinarily somewhat higher." [1]

The significance of these differences in prices appears when it is realized that a reduction of about 7 mills per gallon in the price of illuminating oil would have converted a profit of 10 per cent on the investment in refining and marketing facilities into an actual loss.[2] The differences in price between competitive and noncompetitive towns and areas, even after making liberal allowance for possible differences in production and marketing costs, often amounted, as we have seen, to several cents per gallon. How disastrously the practice of local price discrimination affected the independent refiners must, therefore, be quite obvious.

In carrying out its practice of local price discrimination the Standard Oil Company made frequent use of bogus independent concerns, that is, concerns paraded as independent, yet in

[1] Report on the Petroleum Industry, part II, p. 39.

[2] Ibid., p. 29.

reality controlled by the Standard. By means of these concerns the Standard was able to cut prices to the customers of the independent refiner, without incurring the additional loss involved in a reduction of prices to the entire trade of the territory affected. By this device, also, anti-trust sentiment, which often took the form of a refusal to buy from a trust, was overcome. The government in its Brief presented a list of 63 concerns which had been operated by the Standard as bogus independents.[1] The most extensive of these companies was the Republic Oil Company (a reorganization of the firm of Scofield, Shurmer and Teagle). The chief function of this company, according to the Supreme Court of Missouri, was to follow up the business of the independent refiners, and under the guise of being an independent company, and by means of rebates, fraud, and deception, to wage a most vigorous competition against them in all districts where they competed with the Standard companies. And when, to quote the Court, "the Republic Oil Company had sufficiently chastised the independents, and thereby curbed their desire and ambition to increase the volume of their business, by the reduction of price of oils or otherwise, it would then practically retire from the field of operation and eagerly await the next combat with the independents, if, perchance, any one of them was so timorous as to challenge the monopoly of those two companies [the Standard Oil Company of Indiana and the Waters Pierce Oil Company] by seeking any portion of their trade." [2]

The Standard was able to conduct this policy of local price cutting with effectiveness because of the intimate knowledge it had of its competitors' business dealings. This knowledge was obtained by the Standard Oil Company and its various subsidiary marketing companies through a highly developed system of espionage over the affairs of its competitors. The desired information as to the receipts and shipments of oil by competitors was obtained in part through the observations of its own staff, and in part by bribing railroad employees.[3]

[1] Brief for the United States (no. 725), vol. II, pp. 520–523.

[2] 218 Missouri Reports 445.

[3] Report on the Petroleum Industry, part I, p. 302; and part II, p. 58.

The practice of local price discrimination—a form of predatory competition—was greatly facilitated by the Standard's method of marketing. The Standard had largely eliminated the jobbers, delivering its oil directly to the retailer by means of its own tank cars, tank stations, and tank wagons. This bulk system of distribution has great advantages over barrel or package distribution. In the first place it costs less to ship oil in bulk than in barrels or other packages, and there is often a saving in the local delivery of oil from the railway to the retailer. And perhaps more important is the fact that barreled oil is likely to leak, to cause dirt, bad odors, and fire, and therefore the retail dealer will ordinarily prefer to buy oil from the tank wagon even at a somewhat higher price. Dealing directly with the retailer, and sometimes even directly with the consumer, the Standard could obviously adjust its prices in the various markets in such a way as to stifle threatened competition, as it could not had its product been handled largely through jobbers.

This in itself excellent, because economical, bulk system of distribution further contributed to the maintenance of the Standard's monopoly, in that one tank wagon can serve a given town (if a small one), or a section thereof (if a large one), as well as two can, and at a much less expense per unit of product. This is because of the elimination of a duplicate service. The result is that when once a concern has the facilities for supplying a given town, other concerns naturally hesitate to invade its territory. They well realize that severe competition may result, and in this competition the concern with an established clientele will have the advantage. However, if the first concern to enter the field merely does a local business it will not be able to prevent competitors from gaining a foothold, unless indeed it should be willing to cut prices on all its sales; and this would be quite as costly to it as to its competitors. But if one of the competitors does a nation-wide business, the case is quite different. Thus, the Standard Oil Company, doing business throughout the whole country, could cut prices in the particular localities where there was competition, and could meet the losses thus incurred out of the profits gathered in elsewhere. A concern doing business in a

limited territory must therefore generally succumb in a test of strength with the Standard; and such has been the experience of competition in this industry.

The Standard was thus able to ward off competition in the sale of the greater part of its product. However tempting the prices, independents hesitated to enter Standard markets. They could compete successfully only if able to establish tank stations and tank wagon delivery on a large enough scale to reduce the cost per unit of product to a reasonable figure; and they had learned by bitter experience that if they made the venture the Standard was likely to cut prices below the cost of production and delivery. They realized that the Standard could afford this interminably, if the price cutting was sufficiently localized, and that they could not. It is obvious that only a concern which had strong financial backing, and which sold oil in most of the leading markets of the country, could save itself from the disastrous effects of the practice of price discrimination, and compel the Standard, if that company should determine to put prices below cost, to accept losses as great as its own. And no concern had been able during the period down to the dissolution of the Standard Oil Company in 1911 to develop a business of such a size. The Standard had been able to keep competition localized and scattered, and thus subject to its control. The wonder is, indeed, that competition was not entirely destroyed, unless perchance this was not desired by the Standard from a fear of drastic governmental action.

We have noted the monopolistic position of the Standard Oil Company, and have seen by what means it achieved and maintained this position. How has the consumer fared at the hands of this organization? What has been the course of prices?

The claim has been made that reviewing the history of the oil industry as a whole, the Standard has reduced prices, and thus has benefited the consumer; that because of its remarkable efficiency and the concentration of the business in the hands of a trust the Standard has charged prices lower than would have prevailed under a competitive regime.

Satisfactory data showing the course of prices of petroleum

products in the United States could not be obtained except for comparatively recent years. This was because the Standard for many years had sold its oil for the most part directly to retailers, and it was impossible to obtain from retail dealers, except during recent years, sufficient returns to show the true price movement. However, an idea of the general movement of illuminating oil prices in this country can be gained by a study of export prices, though these export prices must be used with caution. The table below shows the movement of export prices from 1866–1905.

AVERAGE PRICE OF PENNSYLVANIA CRUDE AT WELLS AND AVERAGE PRICE OF EXPORT ILLUMINATING OIL IN BARRELS AT NEW YORK, WITH MARGIN BETWEEN THEM, 1866–1905 [1]

(*Cents per gallon*)

Year	*Pennsylvania crude*	*Export oil in barrels*	*Margin*
1866	6.33	30.08	23.75
1867	4.16	20.75	16.59
1868	6.13	21.16	15.03
1869	10.02	24.59	14.57
1870	8.08	22.96	14.88
1871	9.38	21.69	12.31
1872	7.92	20.97	13.05
1873	3.75	15.71	11.96
1874	2.63	11.65	9.02
1875	2.60	11.39	8.79
1876	5.51	17.22	11.71
1877	5.43	14.71	9.28
1878	2.78	10.75	7.97
1879	2.04	8.09	6.05
1880	2.24	9.15	6.91
1881	2.03	8.07	6.04
1882	1.87	7.42	5.55

[1] Report on the Petroleum Industry, part II, p. 49. The prices from 1866–1878 have been reduced to a gold basis. The export prices are for oil in barrels, and though there has been some fluctuation in the price of barrels independent of that of oil, nevertheless the figures show approximately the price of oil itself.

AVERAGE PRICE OF PENNSYLVANIA CRUDE AT WELLS—*Continued*

(Cents per gallon)

Year	*Pennsylvania crude*	*Export oil in barrels*	*Margin*
1883	2.52	8.13	5.61
1884	2.00	8.29	6.29
1885	2.11	8.09	5.98
1886	1.70	7.11	5.41
1887	1.59	6.73	5.14
1888	2.07	7.49	5.42
1889	2.19	7.12	4.93
1890	2.06	7.31	5.25
1891	1.59	6.93	5.34
1892	1.32	6.07	4.75
1893	1.52	5.23	3.71
1894	1.99	5.19	3.20
1895	3.18	7.36	4.18
1896	2.84	6.97	4.13
1897	1.87	5.91	4.04
1898	2.16	6.32	4.16
1899	3.10	7.98	4.88
1900	3.22	8.46	5.24
1901	2.88	7.51	4.63
1902	2.95	7.38	4.43
1903	3.78	8.69	4.91
1904	3.87	8.30	4.43
1905	3.32	7.22	3.90

From an examination of this table it appears that the margin between crude and refined oil declined almost steadily from 23.75 cents per gallon in 1866 to 11.96 cents in 1873. Prior to 1874 the oil industry was a highly competitive one, and obviously no one concern could claim the credit for the reduction in the margin. The decline in the margin between 1866 and 1873, it should be noted, exceeded the total decline since 1873. This great decline in the margin under a competitive régime—a decline due largely to a reduction in the cost of production—would appear to foreshadow a still further reduction in costs and in the margin, trust or no trust, though not in all probability at so rapid a rate as during the earlier period. Again, it

should be noted that most of the decline in the margin which took place after 1873 had come by 1879. By this time the Standard had obtained its monopolistic control of the industry. The margin had been 11.96 cents in 1873; in 1879 it was 6.05 cents. This reduction in the margin from 1874–1879 was the result in large measure of a decline in transportation costs. The rate on illuminating oil from the Pennsylvania fields to New York, which had been 4 cents per gallon in 1874, fell in 1879, when rates were being slashed, as low as 1 cent per gallon.[1] The building of pipe-lines to the seaboard likewise reduced the cost of transportation, yet, as has been noted above, the Standard did not originate trunk pipe-lines; in fact, it first learned through the successful experiment of the Tide Water Pipe Company that this means of transportation was feasible. The conclusion of the Bureau with respect to the history of prices to 1879 is that the remarkable decline in the margin between crude oil and refined oil was chiefly, if not wholly, due to natural or external causes, quite independent of any special influence of the Standard Oil Company.[2] The Standard, in its opinion, could claim little, if any, credit for the reduction.

The reduction in the margin since 1879 has been noteworthy, yet it has been by no means as great as prior to 1879. In 1879 the margin was 6.05 cents per gallon; in 1905 it was 3.90 cents, though the average for the last five years shown in the table was as high as 4.46 cents. It should be clear that the Standard was not responsible for all of this limited reduction in the margin. Progress in the industry was only to be expected, combination or no combination. Furthermore, the export prices during the period under consideration were not an accurate measure of the domestic prices; domestic prices rose much more rapidly than export prices. The average margin between the quoted price of water-white oil in barrels to jobbers at New York, and the price of Pennsylvania crude in 1882 (the first available year), was 9.2 cents per gallon, while in 1903 it was as high as 10.1 cents per gallon; in 1904 it was 9.8 cents; and in 1905 it was 9.3 cents.[3] This

[1] Report on the Petroleum Industry, part II, p. 50. [2] Ibid.
[3] Ibid., p. 51.

indicates an actual advance in the domestic margin since 1882, but the value of the barrels had increased also, so that an exact comparison between the two periods can not be made.

Such slight reduction as has taken place in the margin since the early eighties has been counterbalanced, moreover, by an increase in the quantity and value of the by-products obtained. That is to say, because of the increase in the value of the by-products the margin should have declined even more than it did. While the Standard has undoubtedly effected greater improvements in the utilization of by-products than have its competitors, to attribute all the improvements to the Standard is, according to the Commissioner, wholly inconsistent with the facts and out of accord with the history of improvements in industries in which competition has been active.[1] It is certain, says the Commissioner, that under free competition, there would have been a sufficient increase in the value of by-products to permit a greater reduction of the margin between crude and illuminating oil than the Standard made. To quote from the report of the Bureau of Corporations, "the Standard has consistently used its power to raise the price of oil during the last ten years, not only absolutely but also relatively to the cost of crude oil." [2]

From this brief analysis of prices, it would appear that the Standard Oil Company has showed as little consideration for the consumer as for its competitors. This conclusion is reënforced by an examination of the profits obtained by the Standard organization.

The profits of the Standard Oil Company have been enormous, both in amount and in proportion to the investment of the company. This becomes apparent upon an examination of the table on page 88.

[1] Report on the Petroleum Industry, part II, p. 51.
[2] Ibid., p. xxx.

DIVIDENDS AND PROFITS OF THE STANDARD OIL TRUST (1882–1899) AND OF THE STANDARD OIL COMPANY (1899–1906) [1]

Year	*Trust certificates or capital stock at end of year. 000 omitted*	*Amount of dividends. 000 omitted*	*Rate of dividends*	*Net earnings. 000 omitted*	*Per cent of net earnings to capital stock*	*Per cent of net earnings to mean net assets*
1882.....	$71,116	$ 3,695	5.25	$12,388	17.4	20.5
1883.....	71,730	4,268	6.00	11,231	15.7	16.3
1884.....	71,230	4,288	6.00	7,778	10.9	10.5
1885.....	71,230	7,479	10.50	8,382	11.8	11.0
1886.....	73,355	7,226	10.00	15,350	20.9	18.7
1887.....	90,187	8,463[2]	10.00	14,026	15.6	15.5
1888.....	90,293	10,236	11.50	12,757	14.1	13.3
1889.....	90,344	10,620	12.00	14,845	16.4	15.0
1890.....	96,941	11,200	12.00	19,131	19.7	17.6
1891.....	97,219	11,648	12.00	16,331	16.8	13.8
1892.....	97,250	11,874	12.21	19,174	19.7	15.4
1893.....	97,250	11,670	12.00	15,457	15.9	11.9
1894.....	97,250	11,670	12.00	15,544	16.0	11.6
1895.....	97,250	16,532	17.00	24,078	24.8	17.3
1896.....	97,250	30,147	31.00	34,077	35.0	23.5
1897.....	97,250	32,092	33.00	47,443[3]	48.8	27.6
1898.....	97,250	29,175	30.00	47,443[3]	48.8	27.6
1899.....	97,250	32,092	33.00	47,443[3]	48.8	27.6
1900.....	97,448	46,691	48.00	55,501	57.0	27.6
1901.....	97,448	46,775	48.00	52,291	53.7	25.1
1902.....	97,448	43,851	45.00	64,613	66.3	29.2
1903.....	97,448	42,877	44.00	81,336	83.5	32.4
1904.....	98,338	35,188	36.00	61,570	62.6	21.7
1905.....	98,338	39,335	40.00	57,459	58.4	18.7
1906.....	98,338	39,335	40.00	83,122	84.5	24.6

[1] Brief for the United States (no. 725), vol. I, p. 6, and vol. II, pp. 8–9; and Report on the Petroleum Industry, part II, pp. 39–40.

[2] Also stock dividend of 20 per cent, amounting to $15,028,200.

[3] There are no data by which to show the earnings of these three years separately; the figures here given show, with substantial accuracy, the average for the three years, 1897–1899. Brief for the United States (no. 725), vol. II, p. 8.

The Standard Oil Company thus paid out in dividends during 1882 to 1906 the sum of $548,436,446, an average of 24 per cent per year. For the ten years ending in 1906, the dividends ranged from 30 per cent to 48 per cent, and averaged 39.7 per cent. Furthermore, a large part of the profits was not distributed to stockholders, but was put back into the business. The total net earnings from 1882–1906 amounted to $838,783,783, exceeding the dividends by $290,347,337. During the ten years ending in 1906, the ratio of net earnings to capital ranged from 48.8 per cent to 84.5 per cent, the average for the ten year period being over 61 per cent.

The rate of dividends and of net earnings becomes even larger, moreover, if applied, not to the capital stock, but to the actual investment in the business, exclusive of the reinvestment of surplus earnings. This investment, determined by adding to the appraised value of the properties in 1882 ($55,710,698) the sums invested since 1882, amounted in 1906 to $69,024,480.[1] Of course, the value of the property held by the Standard in 1906 much exceeded this figure, but this excess value came from the building up of the property through the reinvestment of the surplus earnings. Tested by the investment basis, the Standard Oil Company, with a capitalization in 1906 of $98,338,382, was overcapitalized by about $30,000,000; that is, its stock was watered to that extent.

The objection may be made that the rate of profit on the actual investment is not a fair basis of analysis; that a fairer basis is the ratio of dividends and net earnings to the value of the company's property, i. e., to its net assets. There has, therefore, been included in the table a column showing the per cent of the net earnings to the mean net assets. Naturally these figures are more favorable to the Standard, yet even these figures show how profitable the prices charged by the Standard have been. The net earnings of the Standard for the ten years ending in 1906 averaged over 25 per cent on the company's net assets. It is not necessary to discuss the argument that prices are reasonable when they return only a fair profit on the value of the

[1] Brief for the United States (no. 725), vol. II, pp. 4–5.

property, even including in that value the property which was acquired out of surplus earnings. It is not necessary because viewed from any standpoint it is manifest that the Bureau of Corporations spoke truly when it said that "the domestic consumer has been compelled to pay an exorbitant tribute to the oil monopoly."[1]

It is apparent that the profits of the Standard Oil Company have been enormous. For the ten years ending in 1906 these profits averaged almost $60,000,000 per year, while the dividends averaged nearly $40,000,000 per year. The $20,000,000 of undivided profits were ample to provide for any extension of plant. Much of the $40,000,000 in dividends therefore went into other industries—naturally into those allied with the oil industry. Inasmuch as all industries depend on transportation and as the railroads are large buyers of oil products, intimate affiliations with the railroad companies were well worth cultivating. We find, therefore, that the Standard Oil capitalists became large shareholders in railroad companies. We find also that the Standard Oil interests went into the gas and the electric lighting businesses. The Consolidated Gas Company of New York City, for example, was once, if not still, a Standard Oil affair. We find these same interests in the steel business, notably as large stockholders in the United States Steel Corporation. We find them interested in copper, the Amalgamated Copper Company being a notable example. We find them in the glucose business, particularly in the Corn Products Refining Company. We find that they have even invaded the banking field. In this field they could probably say, with Æneas, *quorum pars magna fui*, a great part of which I—not *was*—but *am*. They could even, with Pistol, exclaim

> Why, then the world's mine oyster,
> Which I with sword will open.

Also in other realms is their influence felt—in the educational world, in religious, humanitarian, and other activities—with the Congress of the United States of America unwilling to

[1] Report on the Petroleum Industry, part II, p. 42.

give a charter to a $100,000,000 of this money, to be devoted in perpetuity to the good of mankind.

Truly, there are various grave and far-reaching problems connected with the question as to whether a monopoly in oil is to be permitted to continue as being on the whole a blessing to mankind, whether a few cents per gallon added to the price of the oil that lights the humbler worker's home or to the price of the gasoline that drives Ford and Packard and business truck is or is not to be hereafter the stable foundation for world-wide business activities and for humanitarian succors as well.

CHAPTER VI

THE AMERICAN SUGAR REFINING COMPANY[1]

The early history of the sugar trust, touched on in chapter III, may be briefly reviewed. The Sugar Refineries Company—a trustee device—had been organized in 1887. In 1890 this arrangement was declared illegal by the New York courts, and as a result a reorganization was determined upon. In January, 1891, the American Sugar Refining Company was chartered in the state of New Jersey,—then a place of refuge for combinations and trusts. The new company had an authorized capitalization of $50,000,000, half preferred stock and half common.[2] The American Sugar Refining Company exchanged its capital stock for the trust certificates of the Sugar Refineries Company, and thus obtained control over the various corporations previously controlled by the trustees. The American Sugar Refining Company next caused the several corporations, seventeen in number, to convey to it their entire property, real and personal; and

[1] On the American Sugar Refining Company see: Original petition in United States *v.* American Sugar Refining Company et al.; Hearings before the Special Committee of the House on the Investigation of the American Sugar Refining Company, 1911–1912; House Report no. 3112, 50th Cong., 1st Sess., 1887–1888; Report of Committee on General Laws relative to "Trusts" and "Sugar Trusts," transmitted to the New York Legislature, April 30, 1891; Report of Joint Committee of the Senate and Assembly appointed to investigate trusts, transmitted to the New York State Legislature, March 9, 1897 (Lexow Report); Industrial Commission, vol. I, pp. 43–166, 801–812; 121 New York Reports 582–626; 156 U. S. 1–46; Report of the Federal Trade Commission on the Beet Sugar Industry in the United States, May 24, 1917; Annual Reports of the Attorney General of the United States, 1909 ff.; Willett and Gray's Weekly Statistical Sugar Trade Journal; Taussig, Some Aspects of the Tariff Question, Part II (Sugar); Vogt, The Sugar Refining Industry in the United States.

[2] Original Petition in United States *v.* American Sugar Refining Company, p. 47. Referred to hereafter as Original Petition.

thereupon dissolved them. Upon the completion of this series of transactions, the American Sugar Refining Company became a property owning trust, as distinct from a holding company trust.

The American Sugar Refining Company operated only four refineries,—the Standard Sugar refinery at Boston, the Matthiessen and Weichers refinery at Jersey City, the Havemeyers and Elder refinery at Brooklyn, and the Louisiana Sugar refinery at New Orleans. These four refineries among them had a daily melting capacity of about 70 per cent of that of the whole country.[1] There were only six other cane sugar refineries in the country, and one of these—the Havemeyers and Elder plant in San Francisco—was for all practical purposes a part of the trust. The owners of the San Francisco plant had gone into the "trust" in 1888, the year after its organization, but because of the opposition of the state of California, the plant had been transferred to Messrs. H. O. Havemeyer, T. A. Havemeyer, and C. H. Senff, members of the board of trustees of the Sugar Refineries Company. These three men had thenceforth carried on the business under the name of Havemeyers and Elder, but always in coöperation with the Sugar Refineries Company, and its successor, the American Sugar *Refining* Company. Including the output of this San Francisco refinery, as is only proper, the American Sugar Refining Company controlled at its organization about 75 per cent of the country's melting capacity.[2]

The only cane sugar refining companies outside of the trust in January, 1891, were the California Sugar Refinery at San Francisco; the Franklin Sugar Refining Company, the E. C. Knight Company, and the Delaware Sugar House, all located at Philadelphia; and the Nash, Spaulding and Company at Boston (later known as the Revere Sugar Refining Company). During the course of the year 1891 the Spreckels Sugar Refining Company began the operation of a large new refinery at Philadelphia; and the Baltimore Sugar Refining Company had under construction a refinery in Baltimore. The sugar trust set out to overcome all these competitors, and by 1892 had acquired all of them but one.

The first to succumb was the California Sugar Refinery at

[1] Original Petition, p. 51.

[2] Ibid., pp. 51–52.

San Francisco, owned by John D., Adolph B., and Claus Spreckels. In March, 1891, in order to bring to an end the competitive campaign which had been instituted against this company by the firm of Havemeyers and Elder, the Spreckels concern entered into an agreement with the firm of Havemeyers and Elder whereby there was incorporated the Western Sugar Refining Company, a California corporation, half of the stock in which was taken by each party. The newly organized corporation, in accordance with the provisions of the agreement, leased for a term of ten years both the Havemeyers and Elder refinery and the Spreckels refinery.[1] Shortly thereafter the Western Sugar Refining Company permanently closed the Havemeyers and Elder refinery, and its former owners sold their plant and their half interest in the Western Sugar Refining Company to the American Sugar Refining Company. The factory continued to be so owned (subject to lease) until 1906, when it was destroyed by fire; and the stock continued to be owned by the American Sugar Refining Company until 1911, when, in accordance with the policy of the new management, the American Company disposed of its stock to the Spreckels interests. By agreement between the American Sugar Refining Company and the Western Company the territory in which each was to sell its products was fixed, and also the prices at which sugar was to be sold.[2]

The control of the Baltimore Sugar Refining Company was effected through purchases of its stock in 1891 and 1892. The factory of this company was never operated; and subsequently it was dismantled, and the company itself dissolved. The purpose was clearly to stifle a prospective competitor. Obviously no economies were effected through the closing of a plant that was never allowed to operate.

In March and April, 1892, the American Sugar Refining Company acquired all but one of the remaining competitors. Up to March of this year competition between the trust and the independents (the Franklin Sugar Refining Company, the Spreckels Sugar Refining Company, the E. C. Knight Company, and the

[1] Original Petition, pp. 52–53. [2] Ibid., p. 54.

Delaware Sugar House) had been severe, and the price of sugar had fallen so low that failure confronted some of these companies. Relief from this contingency was secured by selling out to the trust,—the capitalization of the trust being increased for this purpose from $50,000,000 to $75,000,000. Shortly after 1892 the American Sugar Refining Company consolidated the Spreckels refinery and the Delaware house into one; and the Franklin and Knight refineries into one. In 1897 the Franklin Sugar Refining Company closed its plant, and became simply a selling agency for the Spreckels concern.

By April, 1892, then, the first period of competition with the trust had come to an end. The struggle had been severe, but brief. It ended in the purchase by the American Sugar Refining Company of its leading competitors. In the whole country there were left only two refineries that did not belong to the trust. One of these was the California Sugar Refinery, leased to the Western Sugar Refining Company, half of the stock of which was held by the trust; and the other was the small refinery in Boston owned by Nash, Spaulding and Company,—a plant which the trust had attempted to buy in 1892, but without success. The American Sugar Refining Company produced in 1892, including the output of the California Sugar Refinery, substantially controlled by it, about 98 per cent of the country's output of refined sugar.[1]

But not for long did the American Sugar Refining Company maintain its well-nigh complete monopolistic control of the industry. It immediately took advantage of the situation, and advanced the price of refined sugar until the margin between the raw and refined had much increased.[2] Naturally new refineries were built in order to profit by the higher prices; in fact the history of the trust for a number of years after 1892 was one of constant endeavor to crush or to bring into working relations with it interests that would not sell out.

Already in 1891 the Mollenhauer Sugar Refining Company had been incorporated; and soon after the purchase of the independent refineries at Philadelphia, this company began to oper-

[1] Original Petition, p. 60.

[2] See p. 117.

ate its plant at Brooklyn. In September, 1892,—only a few months after the acquisition by the sugar trust of all the Philadelphia refineries,—the National Sugar Refining Company was organized. In October of the same year the W. J. McCahan Sugar Refining Company was chartered, and in the following year started to refine sugar. To hold this competition within bounds the American Sugar Refining Company in 1893 acquired 30 per cent of the stock of the Mollenhauer concern;[1] and in 1894 it succeeded in effecting agreements with its competitors looking toward a limitation of the output and the fixing of prices.[2] In 1895 the United States Sugar Refining Company was formed for the purpose of constructing a sugar refinery in Camden, New Jersey (just across the river from Philadelphia). But before the plant was ready for operation, the American Company purchased all its stock; and the plant was never completed. In 1897 the California and Hawaiian Sugar Refining Company was incorporated, and in the same year it entered upon the refining of sugar at Crockett, California. This concern refined both cane and beet sugar. Another independent enterprise established in 1897 was the New York Sugar Refining Company, fathered by Claus Doscher, a capable refiner who had disposed of his property to the trust in 1887, and had given up the business. The New York Sugar Refining Company was formed in March, 1897, and its refinery was completed toward the close of 1898. Another very important competitor was Arbuckle Brothers, best known as a coffee house. This firm owned a machine used for filling, packing, and weighing coffee,—a machine which it believed could also be profitably used in the sugar business. In 1893, therefore, it began to buy sugar from the refineries, and to put it up in packages suitable for distribution by wholesale grocers. After some three or four years the firm decided that it would build a refinery of its own; and by the middle of 1898 the plant was in operation.

Competition was thus springing up on all sides, and it was imperative that something be done, unless the sugar trust was to

[1] Hearings on the American Sugar Refining Company, 1911–1912, p. 2924.

[2] House Report no. 331, 62nd Cong., 2nd Sess., p. 4.

abandon its monopolistic purposes. Accordingly, in September, 1898, the American Sugar Refining Company appointed a committee to acquire the factories of any and all independents, this committee being authorized to pay such purchase prices as it might deem fit. In order to facilitate the work of the committee, the price of refined sugar was much reduced. Mr. Jarvie, one of the partners in the firm of Arbuckle Brothers, testified before the Industrial Commission that when his company's refinery was completed in August of 1898, the margin ranged from 80 to 90 cents per hundred pounds; that prices were first cut in September, and that this price cutting continued unremittedly throughout the spring of 1899.[1] At the date of his testimony (June, 1899) the margin was 51 cents per hundred pounds (which was approximately the cost of refining), and the margin had been as low as 32 cents, which was 20 to 30 cents below cost.[2] As a result of this price war Arbuckle Brothers lost a great deal of money—approximately a million and a quarter dollars.[3] Another officer of the Arbuckle firm testified that his company was hard put to it to develop its business because the wholesale grocers in some localities refused to distribute the goods of competitors of the American Sugar Refining Company.[4] This difficulty was obviated in Boston by Arbuckle Brothers dealing directly with the retailers. The latter were given sugar at the same price as the wholesalers, irrespective of quantity; and even as late as 1911 the firm still dealt directly with the retailers in that city.[5] A special retaliatory measure directed against the Arbuckle firm was the invasion by the American Sugar Refining Company of the coffee business. In 1896, having failed in an attempt to buy the patented packing machine of the Arbuckle firm, the American Sugar Refining Company, through Havemeyers and Elder, purchased a large interest in the Woolson

[1] Industrial Commission, I, p. 138.

[2] Ibid.

[3] Hearings on the American Sugar Refining Company, 1911–1912, pp. 1131–1132.

[4] Ibid., p. 1127.

[5] Ibid.

Spice Company of Toledo, at a cost of $1,150 per share, plus commissions.[1] The Woolson Spice Company promptly reduced the price of coffee, and forced the Arbuckle concern to do likewise. But this campaign did not bring about the desired result. The Arbuckle Brothers did not give in, and they are still in the sugar business. Moreover, the American Sugar Refining Company deemed it advisable subsequently to give up its coffee business, the sale of this business being reported by the directors in their annual report to the stockholders in 1909.

The remaining competitors, or "interlopers," as Mr. Havemeyer called them, proved more tractable. Through the formation in May, 1900, of a holding company, organized largely by individuals dominant in the management of the American Sugar Refining Company, the other refiners of cane sugar were brought into harmony with the trust.[2] The name of the holding company was the National Sugar Refining Company of New Jersey, capitalized at $20,000,000, half preferred and half common. The National Sugar Refining Company of New Jersey acquired the entire capital stock of the Mollenhauer Sugar Refining Company, the National Sugar Refining Company, and the New York Sugar Refining Company (also its entire bond issue), giving in exchange therefor $8,250,000 of its own preferred stock. Most of the balance of the preferred stock was used to buy 25 per cent of the stock of the McCahan Sugar Refining Company. The National Sugar Refining Company of New Jersey continued to hold the stocks and bonds of these companies, and managed their affairs in harmony. The common stock of the National Sugar Refining Company of New Jersey ($10,000,000) was given to Mr. H. O. Havemeyer, the president of the American Sugar Refining Company, as promoters' profit.[3] Mr. Havemeyer thereupon

[1] Hearings on the American Sugar Refining Company, 1911–1912, p. 2932, and Lexow Report, pp. 80, 133.

[2] In the case of the California and Hawaiian Sugar Refining Company coöperative relations were not established until 1903.

[3] Original Petition, p. 75, and Hearings on the American Sugar Refining Company, 1911–1912, p. 483.

delivered this stock to himself and to Mr. L. M. Palmer, both of them directors in the American Sugar Refining Company, as trustees under a voting trust for five years, the beneficiaries being Mr. Havemeyer, Mr. Palmer, Mr. W. B. Thomas, Mr. J. E. Parsons, and Mr. J. H. Post, all of them, with one exception possibly, officers in the American Sugar Refining Company.[1] As part of this same set of transactions, the American Sugar Refining Company on its own account acquired $5,128,000 of the preferred stock of the National Sugar Refining Company of New Jersey. (This included the $900,000 of preferred stock in this company received by the American Sugar Refining Company in exchange for the Mollenhauer stock acquired by it in 1893.) The American Sugar Refining Company therefore, either directly or through its officers, held three-fourths of the stock of the newly organized holding company; and as a natural result competition between these concerns was eliminated, except such competition as resulted from Mr. Havemeyer's general policy of promoting competition for business among the several plants. A suit to invalidate the issue of the common stock on the ground that it was made without any consideration and contrary to the laws of New Jersey, was filed in 1911. Mr. Horace Havemeyer, a son of the former head of the American Sugar Refining Company, in testimony before an investigating committee implied that this suit was brought because he (the son) had resigned from the directorate of the American Sugar Refining Company, and proposed to make the National Sugar Refining Company a real competitor.[2] As the result of this proceeding the common stock was cancelled, and the American Sugar Refining Company, owning the majority of the preferred stock, came into direct control of the company. Subsequently it offered to its own shareholders the right to subscribe at par for $5,000,000 of its $5,128,200 stock in the National Company. Many of them refused to make the exchange; and the American Company thus continued to hold nearly one-fourth of the stock in its own treasury.

[1] Original Petition, p. 76.

[2] Hearings on the American Sugar Refining Company, 1911–1912, pp. 569–570.

By 1900, competition, though not eliminated, was clearly held within bounds. The natural consequence was an advance in the price of refined sugar.[1] This, in turn, soon led to the building of competing refineries. Among the new enterprises established were the Federal Sugar Refining Company, the Warner Sugar Refining Company, the Colonial Sugars Company, and the Cunningham Sugar Refining Company.

The American Sugar Refining Company, for its part, continued active in the attempt to eliminate competition. In 1903 the Western Sugar Refining Company, in order to drive out of business the California and Hawaiian Sugar Refining Company (its only rival for the Pacific Coast trade), swamped the markets of the latter with refined sugar sold below the cost of production, with consequent financial loss for the smaller concern.[2] Confronted with bankruptcy, the California and Hawaiian Sugar Refining Company agreed in 1903 that for a period of three years it would not manufacture or sell any refined cane sugar, and that it would permit its beet sugar output to be marketed by the Western Sugar Refining Company.[3] During the life of the agreement, the California and Hawaiian concern refined no sugar of any kind, either from cane sugar or from sugar beets; but it was paid the sum of $200,000 a year, this payment being clearly for the purpose of restraining its competition.

In 1904, also, the American Sugar Refining Company put an end to the proposed competition of the Pennsylvania Sugar Refining Company.[4] This concern had been organized in 1883, with a capital of $100,000. In 1903 its authorized capital was increased to $5,000,000, and the company was nearly ready to begin operating a newly erected refinery. A majority of the stock of the Pennsylvania Sugar Refining Company (26,000 shares out of 50,000) was held by the Champion Construction Company, which, in turn, was controlled by Mr. Adolph Segal. The Construction Company, under contract, was building and equip-

[1] See p. 117.

[2] Original Petition, p. 81.

[3] Ibid.

[4] On this episode see Original Petition, pp. 82–88.

ping the Pennsylvania Sugar Refinery, and it was also building a large apartment house in Philadelphia. It was thus in need of funds. Aware of these facts, Mr. Gustav E. Kissel, an officer and director of the American Sugar Refining Company, acting for the company, lent Mr. Segal the sum of $1,250,000 on a one-year note dated January 4, 1904. As security for the payment of the note when due, Mr. Segal transferred to Mr. Kissel 26,000 shares and $500,000 in bonds of the Pennsylvania Sugar Refining Company, together with written authority to vote the stock, the Champion Construction Company having given its consent to this transaction. The petition of the government charged that Mr. Segal was not aware that the American Sugar Refining Company was the real lender of the money, and that he had no reason to believe that the lender had any ulterior purpose. But Mr. Kissel, controlling, as he did, the Pennsylvania Sugar Refining Company, caused four of the seven directors to resign, and himself and three others to be elected in their stead. Thereupon they had spread upon the minutes a resolution that the refinery be closed. Having prevented the operation of the refinery, which would probably have put Mr. Segal in funds with which to meet the note, Mr. Kissel and the officials of the American Sugar Refining Company succeeded during the years 1904, 1905, and 1906—the petition relates—in so involving Mr. Segal in business complications, and in so embarrassing him, that he found himself unable to pay even the interest on his note; and until 1909 the note remained unpaid and the refinery idle.

Because of this transaction the receiver of the Pennsylvania Sugar Refining Company brought suit against the American Sugar Refining Company under the Sherman law for treble damages. The American Company finally settled by paying $750,000 in cash, and returning the securities.[1] The American Company never got back the principal of the loan, hence the transaction cost it $2,000,000. Counsel for the American Company testified that the settlement was made because the suit was instituted at about the time of the underweighing cases,

[1] Hearings on the American Sugar Refining Company, 1911–1912, p. 220.

and the feeling against the American Company was so strong that the trial would have proven a farce.

In 1908, another independent concern, the Colonial Sugars Company, operating a small refinery in Louisiana, was acquired by the Cuban-American Sugar Company. The latter concern was a combination of several raw sugar producing companies in Cuba, and according to the government petition was operated in harmony with the American Sugar Refining Company, the latter having, in fact, lent it large sums of money, and having in other ways dominated its affairs.[1]

This left as independent cane sugar refineries only Arbuckle Brothers, the Federal Sugar Refining Company, the Warner Sugar Refining Company,[2] the Revere Sugar Refining Company, the Cunningham Sugar Refining Company, and two individual plants, one of which in 1909 was not in operation.

We turn now to the beet sugar industry, and to the attempt of the American Sugar Refining Company to duplicate here the considerable degree of success attained in the cane sugar branch.

The beet sugar industry in this country is comparatively new. Prior to 1898 the production of refined sugar from domestic beets hardly exceeded in any year 2 per cent of the country's output of refined sugar. Under the protection afforded by the Dingley tariff of 1897, however, the industry developed rapidly. In 1901, 7 per cent of the sugar consumed was beet sugar; in 1909, 14 per cent.[3]

Up to 1901 the American Sugar Refining Company had had little to do with the beet sugar industry. In 1897 it had purchased from the Spreckels family a one-half interest in the Western Beet Sugar Company,—a company incorporated in 1887, and possessing a factory in California. In the same year (1897) the two interests had incorporated the Spreckels Sugar Refining

[1] Original Petition, pp. 88–89.

[2] These three companies refined in 1909 some 8.70, 6.30 and 2.50 per cent, respectively, of the country's output. Hearings on the American Sugar Refining Company, 1911–1912, p. 43.

[3] Original Petition, p. 93.

Company, which was to build a new factory in the same state. The following year this newly organized company acquired all of the stock of the Western Beet Sugar Company, and permanently closed the factory. The Spreckels Sugar Company after its organization sold all its product through the Western Sugar Refining Company, one-half of the stock in which, as we have seen, was owned by the American Sugar Refining Company. A half-interest in one concern represented, therefore, the American Sugar Refining Company's total investment in the beet sugar business up to 1901.

The beet sugar industry, however, was steadily growing in importance, and in some localities was becoming a serious competitor of cane sugar. By 1901 there were thirty-one separate concerns manufacturing beet sugar, and eight others were planning to enter the business.[1] The American Sugar Refining Company apparently came to the conclusion that it must eliminate this growing competition. Having obtained the necessary funds by an increase in its capital stock from $75,000,000 to $90,000,000, the company in the summer of 1901 manufactured an unusually large quantity of refined sugar for the purpose, so the government petition alleged, of selling it in the markets of its rivals.[2] About the same time Mr. H. O. Havemeyer and Mr. L. M. Palmer entered into unlawful agreements with various railroads leading out of Boston, New York, Jersey City, Philadelphia, and New Orleans, for the transportation at rates much below the published tariffs of large quantities of refined sugar, and for the free storage of this sugar in warehouses belonging to the railroads.[3] The amount of rebates paid to the American Sugar Refining Company during the years 1901–1904 totalled $500,000.[4] The next step was the sale of this sugar in the markets of the beet sugar companies at prices below the cost of production.[5] This move forced the beet sugar refineries to sell out to the American Sugar Refining Company or face the prospect of ruin; and many of them decided to sell.

[1] Original Petition, p. 96.
[2] Ibid., pp. 97–98.
[3] Ibid., pp. 98–99.
[4] Ibid., p. 99.
[5] Ibid.

The most important concern over which control was secured was the American Beet Sugar Company. This concern, with a capital of $20,000,000, was the leading beet sugar enterprise in the country; it had five plants, and was steadily increasing its business. The American Sugar Refining Company and the American Beet Sugar Company entered in 1902 into a ten-year contract whereby the former was to become the supervising agent for the disposal of the product of the latter at a commission of one-quarter of a cent per pound.[1] The American Sugar Refining Company agreed during the beet sugar season,—beet sugar comes on the market only during a limited period following the maturing of the beet sugar plant,—not to sell sugar in the markets of the American Beet Sugar Company except at its regular open price at the point of production, plus freight. This clause was inserted, according to the vice president of the Beet Sugar Company, to prevent local price cutting by the trust.[2] A drop in the price of refined sugar at the Missouri River from 5 cents to 3½ cents in one day was not competition, in his opinion, but warfare. At about the same time the American Sugar Refining Company acquired $7,500,000 of the Beet Sugar Company's stock. The agreement remained in force until 1907, and the stock continued to be held until 1907 or later; but after 1909 the two companies do not seem to have acted in coöperation.[3] The president of the American Beet Sugar Company testified that the agreement was abrogated on the recommendation of counsel, who advised that the contract, if not cancelled, would land the parties thereto in the penitentiary.[4]

Several other companies were acquired by the sugar trust in the years that followed; but we need not go into the details.[5] Suffice it to say that at high-water mark the American Sugar Refining Company had about $35,000,000 in beet sugar companies, not including the very large personal interest of the

[1] Original Petition, p. 101.
[2] Hearings on the American Sugar Refining Company, 1911–1912, p. 389.
[3] Original Petition, p. 102.
[4] Hearings on the American Sugar Refining Company, 1911–1912, p. 391.
[5] They may be found in Original Petition, pp. 103–132.

various officials of the company—the Havemeyer estate, for example, in 1911 had about $10,000,000 of stock in beet sugar companies.[1] Of the $35,000,000, approximately $12,000,000 was subsequently disposed of, some during Mr. Havemeyer's life, but most of it after his death. Yet even as late as 1911 the company had a majority interest in two beet sugar factories, and a minority interest in thirty-one.[2] The total number of beet sugar factories in the country was 68.[3] The trust, therefore, had some interest in approximately one-half of the factories, and presumably on the whole the more important ones.

Having traced briefly the history of the American Sugar Refining Company's attempt to control the sugar industry, we may next inquire in more detail into the success of its endeavors. To do this with any degree of completeness is difficult; full figures, except for recent years, are not available. Nevertheless it is certain that the company at one time did succeed in effecting practically a complete monopoly, and that subsequently it lost ground materially. It is probable that it does not now control enough of the business to be considered a trust.

The Sugar Refineries Company (the trustee device) produced in 1887 about 78 per cent of the country's output of refined sugar.[4] The next year, after the acquisition of a leading competitor, its proportion increased to about 82 per cent. The American Sugar Refining Company upon its organization in 1891—taking the place of the former "trust"—controlled about 75 per cent of the refining capacity of the country.[5] In 1892 every competitor in the country except one was acquired, and as a result the company produced 98 per cent of the country's output of cane sugar,—the output of beet sugar was a negligible factor at that time. This represented the high-water mark. During the three years 1907–1909, the American Sugar Refining

[1] Hearings on the American Sugar Refining Company, 1911–1912, pp. 559, 2027.

[2] Ibid., p. 42.

[3] Ibid., p. 40.

[4] Original Petition, pp. 38–40.

[5] See p. 93.

Company and its affiliated concerns made, according to the petition of the government, only about 72 per cent of all the refined sugar consumed in the United States not produced from domestic beets; and in 1909 about 70 per cent of the total output of refined sugar, cane and beet.[1] The government in bringing a dissolution suit would not be likely to underestimate the control, hence it is reasonably certain that the sugar trust had lost ground. If we may accept figures presented by the American Sugar Refining Company, before a congressional investigating committee, to prove that the company was not an illegal combination, the company has been unsuccessful in its attempt to control the industry. These figures are shown in the table below.[2]

PRODUCTION OF REFINED SUGAR IN THE UNITED STATES, 1900–1910

Year	*Total quantity refined. Barrels. 000 omitted*	*Quantity refined by American Sugar Refining Co. Barrels. 000 omitted*	*Per cent refined by American Sugar Refining Co.*
1900	13,943	9,378	67.30
1901	14,642	8,482	57.90
1902	16,136	9,193	56.97
1903	15,868	8,767	55.25
1904	16,787	9,748	58.07
1905	16,042	8,484	52.89
1906	17,666	9,014	51.03
1907	18,201	8,966	49.27
1908	19,341	8,731	45.14
1909	19,906	8,588	43.14
1910	21,010	8,853	42.14

This table, prepared by Willett and Gray, would seem to show that the American Sugar Refining Company, at the time when the government brought its dissolution suit (November, 1910), no longer possessed monopolistic control. While in 1900 it produced 67.30 per cent (about two-thirds) of the total quantity of sugar refined in this country, by 1910 it was producing

[1] Original Petition, pp. 139, 142.

[2] Hearings on the American Sugar Refining Company, 1911–1912, p. 43.

only 42 per cent. But these figures hardly portray the real situation. While the table may be accepted as representing truthfully the actual production of the American Sugar Refining Company, it does not show the degree of control exercised by it. For instance, in the production of the company there is included one-half of the output of the Western Sugar Refining Company, in which the American Sugar Refining Company had a one-half interest.[1] But to consider the other half as competitive would be unwarranted. The Western Sugar Refining Company and the American Sugar Refining Company worked together in such harmony that the total output of the Western Company might properly be considered as being controlled by the American Company. Adding the other half of the Western Company's output we get 43.38 per cent in 1910, instead of 42.14 per cent.[2] Again, the American Sugar Refining Company had about one-quarter interest in the National Sugar Refining Company; and the Havemeyer estate held approximately a one-half interest. Up to 1911 the Havemeyers—the only son of Mr. H. O. Havemeyer was a director of the American Company until January, 1911—worked in harmony with the American Sugar Refining Company, and therefore the output of the National Company could hardly be classed as independent.[3] The output of the National Company in 1910 was 11.40 per cent of the total,[4] which being added to the figure of 43.38 per cent would raise the percentage of the American Sugar Refining Company to 54.78. Finally, the American Sugar Refining Company had in 1910 an interest in eleven beet sugar companies, refining 7.43 per cent of the country's output of sugar.[5] Were we to include the production of these concerns, the American Sugar Refining Company controlled in 1910,—the year in which the government brought its suit,—62.21 per cent of the total output.[6] Whether

[1] Hearings on the American Sugar Refining Company, 1911–1912, p. 43.

[2] Ibid., p. 57.

[3] See p. 98.

[4] Hearings on the American Sugar Refining Company, 1911–1912, p. 58.

[5] Ibid., p. 58.

[6] This includes none of the output of the McCahan Sugar Refining Company (producing about 3.0 per cent of the total output), one-fourth of the

this was sufficient to enable it to dominate the industry is open to question. Yet it is clear that the sugar trust was not able to maintain its position against the independent refiners, in spite of the fact that it assimilated from time to time its more vigorous competitors. Moreover, by 1919 the proportion of the American Sugar Refining Company, as calculated by Willett and Gray, had fallen to 27.02 per cent, as compared with 42.14 per cent in 1910.[1] What does this indicate as to the economies of the trust form of organization?

As usual, it is difficult to obtain information as to the nature and importance of the economies effected by the establishment of a trust. Mr. Havemeyer, when asked by the Industrial Commission as to the advantages that resulted from the organization of the sugar trust, replied that the greatest advantage lay in working the refineries full and uninterruptedly. We may quote from his testimony. "If you have a capacity of 140,000,000 and can only melt 100,000,000 somebody has got to cut down materially. The moment you cut down you increase the cost; by buying up all the refineries, burning them up, and concentrating the meltings in four refineries and working them full, you work at a minimum cost. . . .

"Q. So the chief advantage in the combination was in concentrating the production and destroying the poor refineries?

"A. Precisely." [2]

The demand for sugar varies, of course, from time to time, and the American Sugar Refining Company realized a further gain through its practice of adjusting the supply of sugar to the demand by its use of the Brooklyn refinery. The refineries at Boston, Jersey City, Philadelphia, and New Orleans[3] were run to their full capacity practically all of the time, while the output

stock of which was held by the National Sugar Refining Company of New Jersey. Hearings on the American Sugar Refining Company, 1911–1912, p. 43.

[1] See Annual Report of the American Sugar Refining Company, 1919, p. 23.

[2] Industrial Commission, I, pp. 109–110.

[3] The necessity of importing raw sugar has influenced the establishment of refineries at Boston, New York, Jersey City, Philadelphia, Baltimore, New Orleans, and San Francisco.

of the Brooklyn refinery was made to fluctuate according to the state of the market. By this arrangement the loss resulting from a partial output was concentrated on one plant, especially designed for the purpose. It has been estimated that the American Sugar Refining Company through this device effected a saving at times of as much as one-eighth of a cent per pound. Obviously this represents an advantage only when the demand for sugar is so small that all the plants can not be operated at capacity.

According to Mr. Havemeyer the bringing of a number of men into a combination was also advantageous in promoting improvements and more skilful methods; for each man absorbed ideas from the others.[1] The saving in the cost of superintendence, in his opinion, was inappreciable.

The trust also had an advantage, perhaps, in handling labor difficulties. A strike declared at the Brooklyn refinery in the summer of 1910 was defeated, largely because the American Company, having two refineries in reserve, was able to supply the demand for sugar without operating the plant at which the strike occurred.[2]

In spite of these advantages, and perhaps others, the independent refiners have stated most emphatically their belief that they could make sugar as cheaply as the American Sugar Refining Company. Mr. Jarvie, a partner of the firm of Arbuckle Brothers, testified before the Industrial Commission that his refinery was large enough and well enough equipped to secure the advantages of the division of labor as completely as the American Sugar Refining Company; and that the latter could not refine and sell sugar more cheaply than his firm.[3] Mr. Arbuckle testified in 1911 as follows: "We claimed, and I believe the trade claimed, that we had the most economical refinery in the country, and that we could refine sugar as cheap, if not cheaper, than any of them."[4] Mr. Gilmore, of the same con-

[1] Industrial Commission, I, p. 110.

[2] Hearings on the American Sugar Refining Company, 1911–1912, p. 2994.

[3] Industrial Commission, I, p. 139.

[4] Hearings on the American Sugar Refining Company, 1911–1912, p. 2318.

cern, testified that his firm after considerable experimentation had found an output of 7,500 barrels a day to be the most economic unit.[1] When asked whether a sugar refinery had to be enormously large to refine economically, he replied that that was not his experience. The plant might be too large; and thus be cumbersome. An output of 20,000 barrels, for example, would not, in his opinion, show any economy over 7,500 barrels. Furthermore, it did not require a combination of refineries to manufacture sugar economically.

The foregoing testimony of the independents is not regarded as proof of the inability of the American Sugar Refining Company to produce more cheaply than its smaller rivals. The company, for its part, claims just the opposite. In the Annual Report for 1909, for example, the company, referring to the fact that the new refinery at Chalmette, Louisiana (near New Orleans) was equipped with the latest labor-saving machinery, stated that it was expected that sugar could be refined more cheaply at this refinery than at any other in the country.[2] The relative economy of single plants and combined plants thus appears to be a matter upon which the disinterested investigator can as yet do little but speculate.

Such monopolistic control as the American Sugar Refining Company had at the date of the government dissolution suit (1910) was not the result of its ownership of the principal raw material. The acting president of the company introduced as part of his testimony before a congressional investigating committee a statement of the company to the effect that it owned no cane sugar lands, and was not interested directly or indirectly in such lands.[3] A few officials of the company, including the acting president, then owned sugar lands in Cuba, but the testimony was that this sugar was sold to the highest bidder. Of course, the fact that the American Sugar Refining Company was such a large buyer of raw sugar gave it some

[1] Hearings on the American Sugar Refining Company, 1911–1912, pp. 1151–1152.

[2] Ibid., p. 2991.

[3] Ibid., p. 40.

control over the price, but this is quite different from the establishment of a monopoly through the actual ownership of the supply itself.

Neither was the American Sugar Refining Company's power the result of patent rights. The company does not appear to have derived any special advantage through the control of patented machinery.

To what, then, may we ascribe its more or less dominant position?

The record of the trust's relations with the federal government is not one of which it can be proud. The trust has been a noted recipient of tariff favors. Without venturing to discuss the merits of the protective system, it may be said that the sugar duties for many years have been arranged without reference to any legitimate protective principle. The differential on refined sugar under the act of 1883, for example, was considerably greater than the total cost of refining, and this virtually prevented the importation of refined sugar.[1] The prohibitory duty undoubtedly promoted the establishment of the trust in 1887, and enabled it to make enormous profits. In the act of 1890 raw sugar was admitted free (a bounty being given to domestic producers), but the differential on refined was still high enough to shut out foreign competition,[2] and therefore to facilitate the charging of monopoly prices, especially upon the practical elimination of domestic competition in 1892. Hostility toward the sugar trust became intense during the early nineties, and for a time bade fair to lead to the entire removal of the duty on sugar, both raw and refined, in the Wilson tariff act of 1894. Yet it is a matter of history that from this struggle the trust emerged the victor.[3] Duties were somewhat reduced, but they were still more than ample. From 1894 down to the enactment of the Simmons-Underwood bill of 1913, the duties on sugar restrained foreign competition, and thus made it easier

[1] Taussig, Some Aspects of the Tariff Question, pp. 103–104.

[2] Ibid., p. 106.

[3] See Taussig, Tariff History of the United States, fifth edition, pp. 305–314.

for the trust to maintain monopoly prices. Mr. Havemeyer, the head of the sugar trust until his death in 1907, stated before the Industrial Commission that " the mother of all trusts is the customs tariff bill."[1] Though this is certainly not the whole truth,—the causes of trusts lie deeper than this,—it is true that the tariff greatly facilitated the establishment of monopoly conditions in this industry. And no one realized this better than Mr. Havemeyer. The removal of the tariff on refined sugar, he testified, "would kill the sugar industry."[2] . . . "It would inflict a terrible and infamous wrong upon 100,000 people dependent upon it." . . . "It would permit America to be the dumping ground of all the beet sugars of Germany, Austria, France, and Russia." Such action would represent "merely truckling to a miserable clamor—a bugaboo—this babble about trusts."[3] While the tariff was held to be the mother of trusts, Mr. Havemeyer made one exception, and that exception was the sugar refining industry.[4]

Of recent years the situation in this regard has improved. The management of the sugar trust has changed for the better, and little is heard of attempts to dictate tariff legislation. Moreover, the sugar refiners seem to have undergone a change of heart with respect to the tariff on sugar. A high duty on raw sugar makes the growing of sugar beets more profitable, and thus increases the quantity of sugar refined from domestic beets as compared with cane sugar. High duties on raw sugar therefore work against monopoly, since the sources of supply for beet sugar are widely scattered, and the beet factories are small, and consequently hard to control. On the other hand, a low duty on raw sugar—or none at all—makes the growing of sugar beets unprofitable in many sections, and thus stimulates the cane sugar branch. The result is that we find some

[1] Industrial Commission, I, p. 101.

[2] This is denied by Professor Taussig. "The [sugar] refining industry, whether or no it needed protection in earlier days, ceased to need it by the close of the nineteenth century." Some Aspects of the Tariff Question, p. 107.

[3] Industrial Commission, I, p. 115.

[4] Ibid., p. 101.

of the officials of the American Sugar Refining Company in favor of disposing of the beet sugar properties, and of reducing the tariff on sugar.[1]

One of the worst charges that may be made against the American Sugar Refining Company is the fact that, though at times it practically framed the sugar schedule, it sought to avoid payment of the custom duties on raw sugar by tampering with the weighing scales at the ports in such manner as to register false weights. An investigation undertaken by the government in 1907 resulted in a suit against the company to recover the amount of money stolen from the government through false weighing at the Brooklyn plant. The evidence in the suit, according to the Attorney General, revealed a long continued system of defrauding the government, of unparalled depravity.[2] The District Court gave a judgment ordering the company to pay the United States $134,411, representing unpaid custom duties.[3] Thereupon the company opened negotiations with the government, and in 1909 a compromise was made whereby the latter accepted the judgment of $134,411, plus an additional sum of $2,000,000, in full settlement of all civil liabilities of the company for any underweighing at either the Brooklyn refinery or the Jersey City refinery.[4]

The government especially reserved the right to institute criminal prosecutions against the officials responsible for the underweighing. Subsequently suit was brought against the secretary of the company, and the general superintendent of the Brooklyn refinery. Both of them were convicted of fraud; and upon appeal their conviction was sustained by the higher courts.[5] The former was given a sentence of eight months' imprisonment and a fine of $8,000 and costs; and the latter was given two years in jail and a fine of $5,000. Both petitioned for executive clemency, and by order of President Taft the sentence of the

[1] Hearings on the American Sugar Refining Company, 1911–1912, p. 2052.
[2] Annual Report of the Attorney General, 1909, p. 12.
[3] Ibid., p. 11.
[4] Ibid., p. 12.
[5] Ibid., 1910, p. 21; 1911, p. 20; 1913, p. 27.

former was commuted to fine and costs, and of the latter to 30 days in jail.

The importance of these underweighing practices, however, must not be exaggerated. They evidence the cupidity of the sugar companies, or perhaps the desire of their managers to get results (and thus earn their salaries); but even if never discovered, they would not have helped the trust appreciably to maintain its position, except by providing it with the sinews of war. At best, they would merely have enabled it (and the other companies that carried on these practices) to make somewhat larger profits.

The American Sugar Refining Company has also been guilty of other abuses. It has been the recipient of special railroad favors. Freight in the sugar trade is an important item; the territory in which a sugar refining concern can profitably sell depends largely on the freight rates. Both the testimony of officials and the decisions of the courts bear witness to the fact that the American Sugar Refining Company has obtained railroad rebates;[1] in fact, the federal government has collected large sums of money by way of fines for these illegal practices.[2] The company has also made use of local price discrimination, factor's agreements, and covenants restraining sugar refiners from reëntering the field. A special form of competition directed against the beet sugar companies—so the government petition charges—was the practice of erecting beet sugar factories in the neighborhood of proposed independent plants, and of contracting for all the available beets in the neighborhood, thereby making it impossible for the independent factories to engage in manufacture.[3]

The American Sugar Refining Company, up to the death of Mr. Havemeyer in 1907, was a great advocate of secrecy in corporate affairs; and subsequent events made it clear that this policy was adopted mainly because so much was being done

[1] See Hearings on the American Sugar Refining Company, 1911–1912, pp. 301–302, 1419; and 212 U. S. 481–499.

[2] Original Petition, p. 91.

[3] Ibid., p. 147.

that could not bear the light of day. Up to 1907, for example, very little information was given out in regard to the earnings of the company. Mr. Havemeyer, in answer to the queries of the Industrial Commission, stated the philosophy which underlay this attitude of the company. "Q.—Do you believe that these trusts should be put more specifically under governmental control than they are, that they should have examination or inspection similar to the national banks? Mr. Havemeyer.—Not at all. I think the Government should have nothing to do with them in any way, shape, or manner.

"Q.— You think, then, that when a corporation is chartered by the State, offers stock to the public, and is one in which the public is interested, that the public has no right to know what its earning power is or to subject them to any inspection whatever, that the people may not buy this stock blindly?

"Mr. Havemeyer.—Yes; that is my theory. Let the buyer beware; that covers the whole business. You can not wet nurse people from the time they are born until the time they die. They have got to wade in and get stuck, and that is the way men are educated and cultivated." [1]

Of recent years, however, the policy of the company has changed. According to its officials, its policy is to give the greatest possible publicity to its affairs.

Railroad favors and unfair competitive methods thus helped the sugar trust to establish its position. But undoubtedly the greatest source of the sugar trust's strength was its financial ability to buy out those concerns that proved themselves able to compete successfully with it. The tariff wall shut out foreign competition; all that was necessary to retain control was the acquisition of the strongest concerns in this country. During the earlier years of the life of the trust, this policy of buying out competitors proved generally successful, in spite of the persistence of these competitors. But recently, especially with the development of the beet sugar industry, the American Sugar Refining Company has been steadily declining in relative im-

[1] Industrial Commission, I, pp. 122–123.

portance. Apparently it is losing its right to be called a trust. A seeker after truth might properly inquire, why, if the trust form of organization is in fact more efficient, the sugar trust has not held its own against independent refiners, even with the purchase now and then (at excessive figures) of the more aggressive of its competitors? Before accepting industrial monopoly as a natural evolution, he would be justified in asking for more proof of the fact of such economies.

As to the influence of the trust on prices, the former head of the American Sugar Refining Company claimed that the sugar trust had been a benefit to the country; that it had reduced prices to the consumer. As proof, he compared the average margin [1] between raw and refined sugar during the nine years 1879 to 1887—the trust was established in 1887—with the average margin during the eleven years 1888 to 1898. His comparison showed that whereas the margin averaged 1.098 cents during the period prior to the organization of the trust, it averaged only .966 cents during the period subsequent thereto.[2] This proved, it was claimed, that the consumer had benefited by the existence of the trust.

This comparison, however, is not convincing. The period prior to 1887, as the following table shows, was one of high margins during the years 1879 to 1882, but also one of rapidly declining margins. The scale of operations was being greatly expanded, with a consequent lowering of costs; and competition being active, lower prices for refined sugar and lower margins were the natural result. Had Mr. Havemeyer compared the four years 1884 to 1887 with the four years 1888 to 1891 or with the four years 1892 to 1895—the American Sugar Refining Company was organized in 1891—he would have arrived perforce at the opposite conclusion.

A more significant study is the course of prices year by year,

[1] Because of the frequent fluctuations in the price of raw sugar, the significant figure is not the price of refined sugar, but the difference between the price of raw and refined sugar, known as the margin. The margin represents the cost of refining, plus profits.

[2] Industrial Commission, I, p. 103.

interpreted in the light of the facts related in the historical survey. These prices are shown in the table below.

PRICE OF RAW AND REFINED SUGAR, AND MARGIN BETWEEN THEM, 1879 TO 1914 [1]

Year	Raw sugar testing 96°. Per pound	Granulated in barrels. Per pound	Margin	Year	Raw sugar testing 96°. Per pound	Granulated in barrels. Per pound	Margin
1879..	7.423	8.785	1.362	1897..	3.557	4.503	.946
1880..	8.206	9.602	1.396	1898..	4.235	4.965	.730
1881..	8.251	9.667	1.416	1899..	4.419	4.919	.500
1882..	7.797	9.234	1.437	1900..	4.566	5.320	.754
1883..	7.423	8.506	1.083	1901..	4.047	5.050	1.003
1884..	5.857	6.780	.923	1902..	3.542	4.455	.913
1885..	5.729	6.441	.712	1903..	3.720	4.638	.918
1886..	5.336	6.117	.781	1904..	3.974	4.772	.798
1887..	5.245	6.013	.768	1905..	4.278	5.256	.978
1888..	5.749	7.007	1.258 [2]	1906..	3.686	4.515	.829
1889..	6.433	7.640	1.207	1907..	3.756	4.649	.893
1890..	5.451	6.171	.720	1908..	4.073	4.957	.884
1891..	3.863	4.691	.828	1909..	4.007	4.765	.758
1892..	3.311	4.346	1.035 [3]	1910..	4.188	4.972	.784
1893..	3.689	4.842	1.153	1911..	4.453	5.345	.892
1894..	3.240	4.120	.880	1912..	4.162	5.041	.879
1895..	3.270	4.152	.882	1913..	3.506	4.278	.772
1896..	3.624	4.532	.908	1914..	3.814	4.683	.869

During the first four years shown in the table the margin between the price of raw and refined sugar was high. Costs were high, and the margin was necessarily high, if refineries were to make a reasonable profit. During the early eighties, however, as shown elsewhere, sugar refineries were much enlarged; and it became apparent that only those refiners could live who were in a

[1] Industrial Commission, I, p. 103; and Willett and Gray's Weekly Statistical Sugar Trade Journal.

[2] Trust formed the year previous.

[3] In March and April of this year the four Philadelphia refineries were acquired.

position to secure the economics of large-scale *production*. The result of this movement was increased output, lower costs, and reduced margins. The margin had been 1.362 cents per pound in 1879, and 1.437 cents in 1882; by 1887 it had fallen to .768 cents. In October, 1887, the Sugar Refineries Company—a trustee device—became operative, and the next year the margin rose to 1.258 cents, an increase of almost half a cent a pound. Possibly the margin in 1887 was so low that even under competitive conditions it would have subsequently increased, and therefore it may not be correct to ascribe all the advance to the trust. Nevertheless it would seem to be clear that the trust did advance prices in 1888, and that they were higher than they would have been had it not been for the trust. In 1889 the margin continued high, though somewhat less than in 1888. These high prices, however, could not be maintained. The price of refined sugar dropped even more than the price of raw, and the margin in 1890 was only .720 cents, and in 1891, .828 cents. In March and April of 1892, it will be remembered, the four Philadelphia refineries were acquired, and the American Sugar Refining Company produced 98 per cent of the country's output. The margin increased from .488 cents per pound in February to .916 cents in March, and to 1.105 cents in April.[1] The average margin for the year was 1.035 cents in 1892, and 1.153 cents in 1893 (a panic year). These high margins led, even in a period of industrial depression, to the building of a number of competing refineries; and this would seem to explain, in part at least, the lower margins from 1894 to 1897. In 1898 both the Doscher and the Arbuckle refineries began operations. In that year the margin fell to .730 cents, and in 1899 to .500 cents. Mr. Havemeyer testified before the Industrial Commission that the decline in the margin in 1898 was caused by competitors (or "interlopers" as he called them) starting active operations.[2]

The margin for 1899 averaged .50 cents per pound. This was

[1] Jenks, Bulletin of the Department of Labor, vol. V, no. 29, p. 713. For weekly quotations see Report of the Federal Trade Commission on the Beet Sugar Industry in the United States, pp. 108–122.

[2] Industrial Commission, I, p. 108.

undoubtedly below the actual cost of refining. Mr. Doscher testified before the Industrial Commission that refining then cost from .50 to .60 cents per pound, but as a rule about .60 cents.[1] Others placed it at .63 cents, .65 cents, and between .50 cents and .75 cents.[2] Obviously such a low margin could not long continue. In the middle of 1900 the National Sugar Refining Company of New Jersey, controlled by the American Sugar Refining Company and its stockholders, acquired three of the independent concerns, including the Doscher, and the margin went up to .754 cents. The full effect of these acquisitions was not felt, however, until the year 1901, when the margin rose to 1.003 cents per pound. This differential made the manufacture of sugar quite profitable, and as a result new refineries were constructed. By 1902 the margin had fallen to .913 cents. After that date and down to 1914 at least, though there were some fluctuations, the margin showed surprisingly few changes of any importance. Mr. Gilmore, of Arbuckle Brothers, said in 1911 that the margin from 1905 on indicated competitive conditions.[3] There was no longer a sugar war, he said, but a condition of armed neutrality. Each refiner was trying to do the best he could for himself, and meanwhile watching the other fellow pretty closely. The cost of refining cane sugar then ran from about .60 to .65 cents per pound;[4] the margin averaged about .90 cents per pound; and there was left about one-quarter of a cent per pound for profit. The American Sugar Refining Company, gradually losing control of the industry, was unable, apparently, after 1905 to raise the price much, if any, above a competitive level.

The dividends of the American Sugar Refining Company point to monopoly prices during the period when the company was at the height of its power, and to the leveling effect of competition on prices.

[1] Industrial Commission, I, pp. 88, 94.

[2] Ibid., pp. 112, 150; Hearings on the American Sugar Refining Company, 1911–1912, p. 1134.

[3] Hearings on the American Sugar Refining Company, 1911–1912, p. 1140.

[4] Ibid., pp. 1149, 1986, 2260; and Original Petition, p. 34.

Since its organization in 1891 the American Sugar Refining Company has regularly paid 7 per cent on its preferred stock and the following rates on its common stock:

COMMON STOCK DIVIDENDS OF THE AMERICAN SUGAR REFINING COMPANY, 1891–1915

Year	*Per cent*	*Year*	*Per cent*	*Year*	*Per cent*
1891	8	1901	7	1911	7
1892	9	1902	7	1912	7
1893	22	1903	7	1913	7
1894	12	1904	7	1914	7
1895	12	1905	7	1915	7
1896	12	1906	7		
1897	12	1907	7		
1898	12	1908	7		
1899	12	1909	7		
1900	6½	1910	7		

Just how much water there was in the stock can not be stated with certainty. The capitalization of the companies that went into the trust in 1887 was $6,590,000;[1] the amount of trust certificates issued in 1887 and of stock in 1891 was $50,000,000, minus 15 per cent treasury stock. The capitalization of the trust thus exceeded the capitalization of the constituent companies by more than six times. But according to Mr. Havemeyer the constituent companies were undercapitalized; their assets were worth much more than the amount of the capitalization. The Industrial Commission in its review of evidence states that the American Sugar Refining Company, beyond question, was capitalized at a sum at least twice as large as the cost of reconstructing the plants in 1899 to 1900, and the cost of building was then very much higher then than it had been at an earlier date.[2] The value of the brands, which was considerable, must not, however, be overlooked. While an accurate estimate of the extent to which the capital stock of the trust represented property, and the extent to which it represented the hope of monopoly

[1] Lexow Report (1897), p. 384.

[2] Industrial Commission, I, p. 13 (Review of Evidence).

gains, can not be made, there is no doubt that the amount of water was considerable. The Court of Appeals of New York state referred to the stock of the Sugar Refineries Company (the sugar "trust") as being "heavily watered." and "proudly defiant of actual values;"[1] and Mr. Oxnard admitted that when his company joined the trust in 1887 it received $750,000 of trust certificates for property worth $200,000, and capitalized at $100,000.[2]

It is evident that the profits of the American Sugar Refining Company during perhaps the first ten years of its existence were enormous. In 1893, after 98 per cent of the industry had been acquired, the dividends paid on the common stock were 22 per cent—a much larger per cent, as a matter of course, on a reasonable capitalization. From 1894 through 1899, 12 per cent dividends were regularly paid. Since 1900 the profits and dividends have been much less. The company has been unable to charge monopoly prices during the greater part of the period since 1900, and from 1901 to 1915 only 7 per cent was paid on the common,—not so meager, after all, the actual investment being taken into consideration.

It might seem as if the difference between monopoly prices and competitive prices is so small that the matter is not of much consequence to the public. The margin at its highest after the organization of a sugar trust was 1.258 cents per pound (1888); and the normal margin under more or less competitive conditions was about nine-tenths of a cent. The difference, therefore, is only about one-third of a cent per pound. But this small sum amounts to a great deal in the aggregate. The total consumption of refined sugar in the United States in 1915 was 3,648,108 long tons, or 8,171,761,920 pounds. Of this amount, 34.06 per cent, or 2,783,302,109 pounds, was refined by the American Sugar

[1] 121 New York Reports 614, 625.

[2] Hearings on the American Sugar Refining Company, 1911–1912, pp. 371–373. A committee of the House investigating the American Sugar Refining Company declared that the real value of the properties acquired by the trust in 1887 was not over twenty to twenty-five millions. House Report no. 331, 62nd Cong., 2nd Sess., p. 25.

Refining Company. Had the company been able to get one-third of a cent more for its output (as in the halcyon days after the formation of the trust), its profits would have been increased by $9,277,720; and had all this sum been disbursed in dividends, the dividend rate on the (heavily watered) common stock could have been increased from 7 per cent to over 27 per cent.

At this point the presentation of facts respecting this trust may properly close, and the reader may ponder for himself on the problem involved in the collection of a toll (in small amounts from each but enormous in the aggregate) from millions of people by a trust which has been for a generation a noted recipient of tariff favors.

CHAPTER VII

THE AMERICAN TOBACCO COMPANY [1]

The history of the tobacco trust begins with the organization of the American Tobacco Company in 1890. After 1887, attempts had been made to consolidate some of the leading manufacturers of cigarettes, but these efforts proved unsuccessful until 1890.[2] On January 21 of that year the American Tobacco Company was incorporated in the state of New Jersey, with a capital of $25,000,000,—$15,000,000 common, and $10,000,000 preferred.[3] The American Tobacco Company was a consolidation of five of the leading manufacturers of cigarettes, producing

[1] On the tobacco trust see: Report of the Commissioner of Corporations on the Tobacco Industry, part I, Position of the Tobacco Combination in the Industry (February 25, 1909), part II, Capitalization, Investment, and Earnings (September 25, 1911), and part III, Prices, Costs and Profits (March 15, 1915); Original Petition in United States *v.* American Tobacco Company et al.; Transcript of Record, in five volumes, in United States *v.* American Tobacco Company et al. (no. 660), and in American Tobacco Company et al. *v.* United States (no. 661); Brief for the United States in United States *v.* American Tobacco Company et al. (no. 118), and in American Tobacco Company et al. *v.* United States (no. 119); 164 Fed. Rep. 700–728; 191 Fed. Rep. 371–431; 221 U. S. 106–193; Industrial Commission, vol. XIII, pp. 305–342; Report of Joint Committee of the Senate and Assembly appointed to investigate trusts, transmitted to the New York State Legislature, March 9, 1897 (Lexow Report), pp. 860–926, 983–998; Jacobstein, The Tobacco Industry in the United States.

[2] Report of the Commissioner of Corporations on the Tobacco Industry, part I, pp. 64–65. Referred to hereafter as Report on the Tobacco Industry.

[3] The fair value of the tangible assets acquired by the American Tobacco Company was $3,545,108 plus notes of the organizers amounting to $1,825,354, a total of $5,370,462. The balance ($19,629,538) might be regarded as representing good will. The Bureau of Corporations, however, found the good will to be worth only $8,954,892. The overcapitalization, therefore, was very marked. See Report on the Tobacco Industry, part II, p. 8.

in the aggregate 95 per cent of the country's output of cigarettes.[1] It thus possessed a high degree of monopolistic control. The leading concern was W. Duke, Sons and Company, controlled by Mr. James B. Duke. Under Mr. Duke's management the output of this concern had increased from approximately 30,000,000 cigarettes in 1883 to 940,000,000 in 1889.[2] Mr. Duke testified that his company prior to the organization of the combination did about 40 per cent of the cigarette business of the country.[3] The other four concerns had been prospering, and had been increasing their output rapidly.[4] Competition among them, it is true, had been quite vigorous. Very extensive advertising had been resorted to, and large premiums had been given to merchants and consumers. The Duke concern alone had expended $800,000 in advertising and premiums in 1889. These heavy selling expenses had greatly reduced the profits of the five companies, and had undoubtedly promoted the establishment of a combination. But there is little reason to believe that this competition had been ruinous to the parties concerned. The firm of W. Duke, Sons and Company which, according to its president, was worth only about $250,000 in 1885, was worth $7,500,000 in 1889.[5] Certainly the leading concern found the profits enormous, despite the great outlays for competitive purposes.

Having effected a monopolistic position the American Tobacco Company sought to maintain this position by entering into agreements for the exclusive use of the best cigarette machines; in fact, the possibility of acquiring exclusive control over these

[1] 221 U. S. 156.

[2] Transcript of Record in United States *v.* American Tobacco Company (no. 660), vol. IV, p. 335.

[3] Ibid., p. 337. During the ten years prior to 1890 the business of making cigarettes was revolutionized through the introduction of patented machines (Original Petition in United States *v.* American Tobacco Company, p. 13), and this, no doubt, is a partial explanation of the ability of one company to gather to itself such a large percentage of the country's business.

[4] Original Petition in United States *v.* AmericanTobacco Company, p. 14.

[5] Transcript of Record in United States *v.* American Tobacco Company (no. 660), vol. IV, pp. 334, 337.

machines was one of the inducements to the formation of the company.[1] The importance of machinery in the manufacture of cigarettes is made clear by a report of the Commissioner of Labor. In 1876 the labor cost of a cigarette made by hand was 96.4 cents per thousand; in 1895 for the same cigarette made by machinery it was only 8.1 cents per thousand.[2] Among the best cigarette machines was the Bonsack, and the American Tobacco Company almost immediately upon its organization entered into a contract for the exclusive use during a period of three years of the cigarette machines of the Bonsack Machine Company.[3] The Bonsack Company, as a part of the contract, terminated its outstanding agreements with all other manufacturers of cigarettes. This exclusive control of the Bonsack machines was, the Commissioner of Corporations believes, the principal factor in the extraordinary success of the American Tobacco Company from 1890 to 1895.[4] Toward the close of 1895, however, the Bonsack Company, by adverse court decisions, was deprived of its exclusive rights to the most important parts of the machine, and as a result the American Tobacco Company lost the advantage of this artificial prop. The American Tobacco Company likewise secured possession of the patents on the Allison machine, and was thus able to prevent its use by its competitors. Other patents and machines in considerable number were acquired by the American Tobacco Company after its organization, the purpose in some cases being to utilize these patents and machines, in other cases to prevent their utilization by competitors.

In addition to the endeavor to maintain its position by monopolizing the machinery for the manufacture of cigarettes, the cigarette trust employed another policy,—a policy which it continued throughout its whole career. This was the acquisition, at high prices if necessary, of its most vigorous competitors. Cigarette companies in considerable numbers were acquired

[1] Report on the Tobacco Industry, part I, p. 64.

[2] Thirteenth Annual Report of the Commissioner of Labor (1898), p. 73.

[3] Report on the Tobacco Industry, part I, pp. 67, 266.

[4] Ibid., part I, p. 266.

after 1890, as a means of retaining the monopolistic position originally attained.[1] The plants thus acquired were generally closed; and the brands, though sometimes utilized, were usually withdrawn.[2] Frequently the owners of the plants acquired were compelled to sign an agreement not to reënter the tobacco business again for a number of years.[3]

The next trust in the tobacco industry was formed in the plug branch. By the purchase of the National Tobacco Works in 1891 the American Tobacco Company had acquired several popular plug brands. In 1893, Mr. James B. Duke, president of the American Tobacco Company, endeavored to engineer a combination of plug tobacco concerns.[4] Not proving successful in this, the American Tobacco Company in 1894 began an aggressive campaign for the control of the plug business. As a part of the competitive warfare, prices were cut below cost.[5] The principal brand made use of in this fight was appropriately termed "Battle Ax." In 1891 this brand had retailed at 50 cents per pound; in 1894 the price was reduced to 30 cents.[6] This policy of price cutting was accompanied by an advertising campaign, which was pushed most vigorously in the territory of the leading competitors. In some sections, indeed, agents of the American Tobacco Company presented every man they met with a free sample of "Battle Ax." By such means, the American Tobacco Company, aided as it was by the advantages enjoyed through its control of the cigarette trade, was able to increase its sales of plug tobacco from 9,000,000 pounds in 1894 to 38,000,000 pounds in 1897; and its proportion of the total production from 5.6 per cent to 20.9 per cent.[7]

[1] For an account of the cigarette concerns acquired from 1890–1904, see Report on the Tobacco Industry, part I, pp. 67–71, 79–93.

[2] Brief for United States in United States *v.* American Tobacco Company (nos. 118, 119), p. 9.

[3] Testimony of Mr. James B. Duke before Industrial Commission, XIII, p. 323.

[4] Original Petition in United States *v.* American Tobacco Company, p. 25.

[5] 221 U. S. 160.

[6] Report on the Tobacco Industry, part I, p. 96.

[7] Ibid., pp. 97–98.

This expansion of its operations, however, was expensive. During the four years from 1895 to 1898, the American Tobacco Company sustained losses on its plug business amounting to more than $3,300,000.[1] This competition was ruinous, especially to the concerns unable to make up their losses in the plug branch out of the enormous profits of the cigarette branch. It was ruinous, not because competition is naturally or inevitably ruinous, but because the cigarette trust was deliberately manœuvring to force the manufacturers of plug tobacco into a combination. By early in 1898 the outside manufacturers had been brought into the proper frame of mind; they had come to favor a combination as a means of obtaining relief from the attacks on their business. The first plan for a combination fell through, however, partly because the promoters feared that the Spanish-American War, with its increased revenue taxes, would seriously affect the profitableness of the combination. The American Tobacco Company thereupon, in the fall of 1898, purchased two more important plug companies, and apparently was about to give its rivals another taste of cutthroat competition. These purchases undoubtedly hastened the movement for the establishment of a combination of the leading plants. By October, 1898, the definite announcement was made that a consolidation of the leading plug plants would be formed, including those owned by the American Tobacco Company. The name of the consolidated company was the Continental Tobacco Company; and it was incorporated in New Jersey on December 10, 1898, with an authorized capital of $75,000,000.[2] The new plug combination embraced nearly every important navy plug concern in the country, including the firm of P. Lorillard.[3] But the combination did not include the Liggett and Myers Tobacco Company, possessing the largest single plant of any plug concern. And without the Liggett and Myers plant the Continental Tobacco Company could hardly carry out its purpose, which was

[1] Report on the Tobacco Industry, part I, p. 367.

[2] Ibid., pp. 99–100.

[3] Ibid. For an explanation of the terms "navy" plug and "flat" plug, see Report on the Tobacco Industry, part III, pp. 45–46.

the monopolization of the plug business. This fact was clearly realized, and the attempt was consequently made to acquire this concern, though at first without success.

The inability to secure control of this company was due to the opposition of an element in its management which had planned a raid on the plug combination. In October, 1898, a syndicate, consisting of Mr. Thomas Fortune Ryan, Mr. P. A. B. Widener, and Mr. Anthony N. Brady, among others, acquired the National Cigarette and Tobacco Company, the only real rival of the American Tobacco Company in the cigarette business.[1] In the same month the syndicate organized the Union Tobacco Company of America; and this company took over the stock of the National Company. In December, 1898, the Union Tobacco Company purchased 86 per cent of the stock of the Blackwell's Durham Tobacco Company, one of the leading independent smoking tobacco concerns. Early in 1899 it became known that the organizers of the Union Tobacco Company held an option on a majority of the stock of the Liggett and Myers Tobacco Company. The men who had promoted the Union Tobacco Company apparently reasoned that a powerful concern standing outside the combination would be in a position to exact a good price as a condition of joining it; and the company was clearly strong enough financially to cause great loss to the combination, should a struggle actually take place. This fact was well realized by the dominant interests in the cigarette and plug combinations, and in 1899 the Continental Tobacco Company purchased at a very high figure the Union Tobacco Company, and with it secured the Liggett and Myers concern.[2] Mr. Duke testified subsequently that the purpose in buying the Union Tobacco Company was to bring into the fold the wealthy financiers who had promoted it; that the American Tobacco "crowd" was not strong enough financially.[3] As a matter of fact, the men who controlled the Union Tobacco Company did shortly there-

[1] Report on the Tobacco Industry, part I, pp. 73–74.

[2] Ibid., p. 100.

[3] Transcript of Record in United States *v.* American Tobacco Company (no. 660), vol. IV, p. 367.

after enter the directorate of either the American Tobacco Company or the Continental Tobacco Company, and they became thenceforth very important factors in the control of the whole Tobacco Combination. With the acquisition of Liggett and Myers the Continental Tobacco Company produced 56.3 per cent of the country's output of plug tobacco; and thus attained a considerable degree of monopoly control,—a control later much increased.[1] From the outset the Continental Tobacco Company was dominated by the American Tobacco Company interests, though the American Tobacco Company itself held only about one-third of the company's stock.[2] Such stock as it held it had received in exchange for the plug business which it had developed, and which it had turned over to the Continental Tobacco Company.

The formation of the Continental Tobacco Company, dominated as it was by the American Tobacco Company, added greatly to the Combination's control of the smoking tobacco business. From the very beginning the American Tobacco Company had produced some smoking tobacco; it had inherited this business from its constituent concerns, each of which manufactured several brands of smoking tobacco. In 1891 two additional smoking tobacco concerns were acquired. As the result of these purchases the American Tobacco Company produced in 1891, 18 per cent of the country's output of smoking tobacco. During the next few years, the plug business especially was being developed; and by 1897 the American Tobacco Company, despite several acquisitions, had increased its proportion of the smoking tobacco business to only 22.7 per cent. However, several of the companies acquired by the Continental Tobacco Company in 1898 and 1899 produced smoking tobacco as well as plug, and the result was that by 1900 the combined production of the American Tobacco Company and the Continental Tobacco Company amounted to 59.2 per cent of the total output. This

[1] Report on the Tobacco Industry, part I, p. 365. For an account of the acquisitions of the Continental Tobacco Company from 1899–1904, see Report on the Tobacco Industry, part I, pp. 103–113.

[2] Ibid., p. 102.

gave the Tobacco Combination a very strong hold on this branch,—a hold which was subsequently extended.

Another branch in which the Combination increased its business was the production of fine-cut tobacco,—a form of tobacco used for chewing. From 1890 to 1898 the production of fine-cut tobacco by the Combination was very small; it never exceeded 6 per cent of the total.[1] But with the organization of the Continental Tobacco Company, several of whose constituent companies produced considerable amounts of fine-cut tobacco, and with several minor acquisitions about the same time by the American Tobacco Company, the Combination's percentage of the business had increased by 1900 to 50.5 per cent,—a percentage greatly increased subsequently.

Shortly after the organization of the Continental Tobacco Company, the dominant interests in the cigarette and plug trusts organized a snuff trust. Since 1891 the American Tobacco Company had produced a small quantity of snuff, and in 1899 it purchased some additional snuff concerns. The Continental in 1898 had acquired the large snuff business of P. Lorillard and Company. The American and Continental companies between them sold in 1899 about 32 per cent of all the snuff sold in the country.[2] This, however, was well under the sales of the Atlantic Snuff Company, a combination in 1898 of four concerns producing among them 46.5 per cent of the total output of snuff.[3] To get control of the snuff business, therefore, it was necessary to wage a competitive campaign against the snuff combination. In 1899, then, the American and Continental Companies greatly reduced the price on some of the leading brands of snuff, in the face of a doubling of the internal revenue tax; and they also gave away large quantities of snuff to prospective customers. The snuff combination followed suit, and until early in 1900 competition was quite vigorous. A combination was then decided upon. On March 12, 1900, the American Snuff Company was incorporated in the state of New Jersey. It took over the snuff busi-

[1] Report on the Tobacco Industry, part I, p. 408.
[2] Ibid., part III, p. 138.
[3] Ibid., part I, p. 141.

ness of the Atlantic Snuff Company, the American Tobacco Company, the Continental Tobacco Company, and the George W. Helme Company.[1] The output of the American Snuff Company in 1901, its first full year's business, amounted to 80.2 per cent of the total output of snuff.[2] It thus secured a monopolistic position in the industry,—an accomplishment that was facilitated because of the fact that the greater part of the business was already concentrated in the hands of a few concerns. Over 43 per cent of the stock of the American Snuff Company at its organization was given to the American Tobacco Company and to the Continental Tobacco Company in exchange for their snuff business.[3] This was only a minority, but in view of the fact that large stockholders of the American Tobacco Company also held stock in the American Snuff Company it amounted to control.

By 1900, therefore, the Tobacco Combination had reached a dominant position in the manufacture of all the important branches of tobacco except cigars. It produced 92.7 per cent of the output of cigarettes; 62 per cent of the plug tobacco; 59.2 per cent of the smoking tobacco; 50.5 per cent of the fine-cut tobacco; and 78.0 per cent of the snuff (80.2 per cent in 1901).

The Combination next directed its attention to the cigar business, the most important of all the branches of tobacco manufacture.[4] The American Tobacco Company had entered the cheroot branch of cigar making in 1891 by the purchase of the business of P. Whitlock, the manufacturer of "Old Virginia Cheroots"; but for some time thereafter it made no ordinary cigars. Shortly after the organization of the Continental Tobacco Company, the American Tobacco Company made plans to engage in the manufacture of cigars. As the first step in that direction, it began experimenting with cigar making machines;

[1] Report on the Tobacco Industry, part I, pp. 143–144. The subsequent acquisitions of the company are shown on pp. 146–148.

[2] Ibid., part III, p. 138.

[3] Ibid., part I, p. 143.

[4] The value of cigars in 1904 was almost 60 per cent of the total value of all the manufactured products of tobacco. Report on the Tobacco Industry, part I, p. 50.

its control of the machines for making cigarettes had shown it the advantage of producing with the aid of machinery, and of controlling the patents on the machinery. But no particular success crowned its efforts in this direction; and even to-day machinery is not much used except in the manufacture of the cheaper grades of cigars.[1] In spite of its lack of success, in this direction, however, it determined to organize a cigar company, and to go after the cigar business. Accordingly on January 12, 1901, the American Cigar Company was incorporated in the state of New Jersey.[2] Over 70 per cent of its stock was subscribed to by the American Tobacco Company and the Continental Tobacco Company. The American Cigar Company took over the greater part of the cheroot and little cigar business of the American Tobacco Company, and soon purchased a number of cigar concerns, including the Havana-American Tobacco Company, itself a combination of cigar companies. These acquisitions made the American Cigar Company the largest manufacturer of cigars in the country; in 1901 it produced 10.9 per cent of the total output of cigars (not including little cigars).[3] During 1901–1903 the American Cigar Company made a determined attempt to monopolize the business. Prices were reduced, cigars given away, an extensive advertising campaign carried on, and expensive retail stores fitted up.[4] By such means the leading interests in the Tobacco Combination apparently hoped to duplicate their success in the other branches. But this campaign proved unsuccessful. Enormous losses were incurred, and though the output of the American Cigar Company was considerably increased, it manufactured only 16.4 per cent of the total output in 1903, and even less in the years that followed.[5]

The explanation of this failure to control the industry is not hard to find. In the manufacture of such products as cigarettes,

[1] Report on the Tobacco Industry, part I, p. 6.

[2] Ibid., p. 151.

[3] See p. 144.

[4] Report on the Tobacco Industry, part I, p. 420.

[5] See p. 144.

plug tobacco, and smoking tobacco, machinery is extensively used. Even before a combination was formed, there was a decided concentration of the business in the hands of a few concerns; and to bring together these concerns was not particularly difficult, especially in the face of the pressure that was brought to bear on the recalcitrant. But then (as now) a very large proportion of the cigars was made by hand. Even when machinery was used, it was of much less importance than in the other branches of tobacco manufacture. Because of the fact that machinery played little part, small establishments were at no great disadvantage as compared with large ones. A cigar factory could be started with small capital, and naturally there were—and are—a great many plants. For these reasons it was difficult to establish an effective cigar combination, and even if one should be established it would prove well-nigh impossible for it to maintain control of the industry. Economic conditions in this branch of the trade have thus been such as to thwart the designs of the trust promoters.

The next important combination in the tobacco industry was the Consolidated Tobacco Company, a holding company organized on June 5, 1901, to unite the American Tobacco Company and the Continental Tobacco Company,—the two principal companies in the Tobacco Combination. Immediately upon its organization the Consolidated Company, promoted by some of the leading financial interests in the tobacco combinations, offered to exchange its 4 per cent bonds in equal amounts for the common stock of the Continental Tobacco Company, and at the rate of 2 to 1 for the common stock of the American Tobacco Company.[1] This offer was generally accepted by the stockholders. The result was to give more complete control over the business to the few financiers who already rather effectively controlled the management. At the time, the exchange of their common stock for the bonds of the holding company had seemed to the stockholders to be quite profitable. The common stock of the Continental Tobacco Company had never borne a dividend, and during a considerable period had sold below $30 per share;

[1] Report on the Tobacco Industry, part I, pp. 114–115.

the holders were now assured 4 per cent regularly.[1] The common stock of the American Tobacco Company, highly watered as it was, especially since the declaration of a 100 per cent stock dividend in 1899, paid only 6 per cent, and was earning about 9 per cent.[2] By the exchange an 8 per cent return was practically guaranteed. Yet the organizers and *stockholders* of the Consolidated Tobacco Company made enormous profits. They apparently believed that the profits of the business would be much greater in the future than they had been up to that time. One reason for this belief was the probable removal of the Spanish-American War taxes on tobacco products, and the conviction that it would not be necessary, in view of the control the Combination possessed over the industry, to reduce prices by the amount of the tax.[3] As a matter of fact, the taxes were removed, and the profits did increase enormously. And these profits largely went, of course, not to the bondholders, but to the few men who held the stock of the Consolidated Tobacco Company. Over half of the stock of this company, in fact, was held by six men,—Messrs. James B. Duke, Anthony N. Brady, Oliver H. Payne, Thomas F. Ryan, P. A. B. Widener, and William C. Whitney.[4] Inasmuch as the Consolidated Tobacco Company controlled the American Tobacco Company, these six men dominated the whole Tobacco Combination.

The main reason for the formation of a holding company seems to have been to effect the concentration of control just described. Another purpose, however, was to obtain additional capital in order to expand the business of the Combination. One direction which this expansion took was the foreign trade.

Since its formation (1890) the American Tobacco Company had had a considerable foreign trade, mainly in cigarettes. During the nineties it extended this trade considerably. As an aid in selling its exported cigarettes, and to secure the advantages of production near the market, it acquired several companies in foreign countries, including Germany, Japan, Australia, and Canada. In the fall of 1901, the necessary cash being supplied by

[1] Report on the Tobacco Industry, part I, p. 120.
[2] Ibid., p. 121.
[3] Ibid., pp. 124–125.
[4] Ibid., p. 119.

the organization of the Consolidated Tobacco Company, a decision was made to compete more vigorously for the English trade. As the first step in this program, the American Tobacco Company acquired in September, 1901, the firm of Ogden's (Limited), one of the leading tobacco manufacturing concerns in the United Kingdom.[1] This invasion of their field caused great alarm among the other British manufacturers of tobacco, and to protect themselves against the powerful American company thirteen of the leading manufacturers united in December, 1901, to form the Imperial Tobacco Company. The British combination at once inaugurated a campaign to drive out the American concern. Large bonuses were offered to such customers as would agree not to handle American goods for a period of years. The American Tobacco Company, through the Ogden's concern, retaliated by promising to its British customers all of its net profits for the following four years, and in addition £200,000.[2] The Imperial Tobacco Company then threatened to meet the American Tobacco Company in its own territory, and during the summer of 1902 was reported to be choosing locations for its American plants. But in September, 1902, before this threat was carried out, an agreement was entered into which brought the struggle to an end.

By this agreement the American Tobacco Company and its allied concerns transferred all their business in Great Britain and Ireland to the Imperial Tobacco Company.[3] This included, of course, the firm of Ogden's. The Imperial Tobacco Company, for its part, agreed not to manufacture or sell tobacco in the United States, except through the American Tobacco Company, though it reserved the right to buy tobacco leaf in the United States for its business in Great Britain. The American Tobacco Company and the Imperial Tobacco Company then united in the organization of a new corporation to handle the tobacco trade in the countries outside of the United States (and its noncontiguous

[1] Report on the Tobacco Industry, part I, p. 166.

[2] Ibid., p. 169.

[3] A copy of the agreement is in the Report on the Tobacco Industry, part I, pp. 431–447.

territories) and Great Britain. The American Tobacco Company received two-thirds of the stock of the new company, and the Imperial Tobacco Company one-third. The British-American Tobacco Company (the new concern) was incorporated in Great Britain in 1902, and it acquired all the foreign business of the American and Imperial Companies. It was provided that the British-American Tobacco Company could engage in the manufacture of tobacco products in the United States or Great Britain, but solely for the purpose of engaging in the export trade. After this agreement was entered into the British-American Tobacco Company rapidly developed its business in foreign countries, with the result that it established itself in almost every country where the manufacture of tobacco was not a government monopoly.

The Tobacco Combination was controlled until 1904 by the Consolidated Tobacco Company. But on October 19, 1904, the Consolidated Tobacco Company and its two subsidiary concerns (the American and the Continental) were merged into a single company,—the American Tobacco Company.[1] This new company, until the dissolution in 1911, remained the dominant concern in the Combination.

There were several reasons for the change in organization. In the first place, the Northern Securities decision, rendered in 1904, raised grave doubts as to the legality of the Consolidated Tobacco Company, which, like the Northern Securities Company, was a holding company. Secondly, it was hoped to improve the market for the bonds of the Consolidated Tobacco Company. These bonds had always sold at a low figure. By exchanging a part of these bonds for 6 per cent preferred stock in a new company it was believed that the market for the remaining bonds would be improved. Thirdly, the insiders desired to concentrate the control of the entire business more fully in the hands of the common stockholders.[2] Prior to the merger of 1904, the preferred stocks of the American and Continental Companies, which were largely held by the outsiders, had voting power, although not enough to outvote the common stock in these com-

[1] Report on the Tobacco Industry, part I, p. 128. [2] Ibid., p. 129.

panies held by the Consolidated Tobacco Company. But by the exchange of this preferred stock for bonds in the reorganized American Tobacco Company, and by the issuance by the latter company of new 6 per cent nonvoting preferred stock, given in exchange for part of the 4 per cent bonds of the Consolidated Tobacco Company, the power of the insiders in the Combination was made even more secure than it had been.

After the merger in 1904 the same methods that had been used from the beginning continued to be employed. This, the Supreme Court held, was indisputably established by the record. Competitors were acquired; restrictive covenants against engaging in the tobacco business were taken from the sellers; and plants were purchased, not to operate, but in order that they might be dismantled.[1]

The American Tobacco Company, the controlling factor in the whole Tobacco Combination, was controlled by a very few individuals. At the end of 1906 this company had a total capitalization of $235,191,950, but of this amount only the common stock, representing about one-sixth of the total, had any voting power for the election of directors, or for the ordinary affairs of management. The great bulk of the common stock was owned by the directors and their associates. The twenty-eight directors and four other stockholders together owned 77 per cent of the common stock; indeed, the ten largest stockholders, six of whom were directors, together owned 63 per cent of all the common stock.[2] And since the American Tobacco Company (the 1904 corporation) held a large part of the stock of the trusts or combinations in the other branches of the tobacco business—the American Snuff Company, the American Cigar Company, the British-American Tobacco Company, and a vast number of other concerns—the control of the whole Tobacco Combination rested in the hands of a very small number of persons.[3]

The historical development of the various tobacco combina-

[1] 221 U. S. 174–175.

[2] Report on the Tobacco Industry, part I, pp. 202–203.

[3] For a list of the subsidiary companies in the Tobacco Combination in 1906, see Report on the Tobacco Industry, part I, pp. 212–218.

tions and trusts has been briefly outlined. It has been seen that these combinations upon their establishment generally possessed a high degree of control over the industry. To what extent was this control maintained? From lack of more recent reliable data we must make use, for the most part, of the figures contained in the reports of the Commissioner of Corporations on the Tobacco Industry.

The position of the tobacco trust in the cigarette and little cigar business combined for the years 1891–1906 is shown in the following table (the records of the Bureau of Internal Revenue do not show the production of these products separately until 1898):

TOTAL OUTPUT OF CIGARETTES AND LITTLE CIGARS, AND PROPORTION THEREOF MADE BY THE TOBACCO COMBINATION, 1891–1906 [1]

Year	*Output. 000,000 omitted*	*Per cent made by Combination*	*Year*	*Output. 000,000 omitted*	*Per cent made by Combination*
	Number			*Number*	
1891 ..	3,137	88.9	1899 ..	4,367	89.0
1892 ..	3,282	87.9	1900 ..	4,255	88.1
1893 ..	3,660	85.3	1901 ..	4,505	87.1
1894 ..	3,620	86.5	1902 ..	4,820	82.8
1895 ..	4,237	87.3	1903 ..	5,327	82.1
1896 ..	4,967	83.4	1904 ..	5,881	86.6
1897 ..	4,927	80.0	1905 ..	6,309	83.9
1898 ..	4,842	84.6	1906 ..	7,427	82.3

In 1891 the trust produced 88.9 per cent of the cigarettes and little cigars made in this country. In 1892 and 1893 its proportion declined, reaching 85.3 per cent in the latter year. This was in spite of the acquisition in 1892 of the large cigarette business of Hernsheim Brothers. By 1895, largely through the purchase of three of the most important little cigar concerns in the country, the trust had increased its control to 87.3 per cent. The next year the Drummond Tobacco Company and the Liggett and Myers Tobacco Company, plug manufacturers with plants

[1] Report on the Tobacco Industry, part I, p. 325.

in St. Louis, engaged on a large scale in the manufacture of cigarettes, as a measure of retaliation against the American Tobacco Company, which was then conducting its destructive campaign for the plug business. As showing the importance of these concerns, the cigarette output at St. Louis increased from twenty million cigarettes in 1895 to three hundred and eighteen million in 1896. In 1897 the sales of the American Tobacco Company actually declined. The result was a reduction in its output from 87.3 per cent in 1895 to 80.0 per cent in 1897. The competitors of the cigarette trust had thus given a very good account of themselves. But in 1898 the Drummond Tobacco Company was acquired by the American Tobacco Company, and in 1899 the Liggett and Myers concern came into the fold; and as a result the percentage of the American Tobacco Company rose from 80.0, to which it had fallen in 1897, to 89.0 in 1899. From then on until 1903 the proportion of the trust declined steadily, falling to 82.1 per cent in 1903. In 1904 the percentage increased to 86.6, in part because of the acquisition of competitors; but by 1906 had fallen to 82.3. Though greatly increasing its output since 1891, the trust did not quite hold its own, and had it not been for the purchase of the leading competitors, would undoubtedly have lost very heavily; in fact, it is quite likely that it would have found itself unable to maintain its monopolistic position.

Since 1898 the figures are available for cigarettes and little cigars separately. The important data with respect to cigarettes are shown in the table on page 140.

The table calls for little comment. The acquisition of the Drummond, and the Liggett and Myers concerns in 1898 and 1899 added considerably to the trust's proportion of the cigarette business; and by 1899 it was producing 94.7 per cent of the total. From then until 1907 its percentage declined every year, with the exception of 1904. The increase in 1904 was due in large measure to the acquisition in the preceding year of the Wells-Whitehead Tobacco Company. The steady increase in the cigarette business of the independents up to 1907 can be explained in part by the growing preference on the part of the

TOTAL OUTPUT OF CIGARETTES, AND PROPORTION THEREOF MADE BY THE TOBACCO COMBINATION, 1898–1910 [1]

Year	*Output.*[2] *000,000 omitted*	*Per cent made by Combination*
	Number	
1898.....	4,385	88.3
1899.....	3,744	94.7
1900.....	3,644	92.7
1901.....	3,730	89.9
1902.....	4,144	84.6
1903.....	4,735	83.9
1904.....	5,145	87.7
1905.....	5,505	84.7
1906.....	6,437	82.5
1907.....	7,077	81.7
1908.....	7,351	81.8
1909.....	8,500	83.6
1910.....	9,985	86.1

public for Turkish cigarettes. These, except for the cheaper grades, were largely made by hand, and this naturally helped the smaller concerns. The independents, principally Turks, Greeks, and Egyptians, produced about half of all the Turkish cigarettes made in this country.[3] After 1907, however, the independents lost ground relatively; by 1910 the trust was producing 86.1 per cent of the total output.

The figures just given are for the output of this country. The Tobacco Combination, however, was a large exporter of cigarettes—it was, in fact, practically the only exporter—and its proportion of the output produced for domestic consumption was somewhat less than its proportion of the total output. Thus, whereas in 1908 it had produced 81.8 per cent of the country's output of cigarettes, it produced only 76.7 per cent of the cigarettes entering into domestic consumption.[4]

After 1898 the Tobacco Combination greatly increased its

[1] Report on the Tobacco Industry, part III, p. 153.
[2] Includes quantities in bonded warehouses for export.
[3] Report on the Tobacco Industry, part I, p. 334.
[4] Ibid., p. 329; and part II, p. 43.

control over the little cigar branch. In 1898 it had produced less than half of the little cigars; by 1910 it produced over nine-tenths.[1] This strengthening of its position can be ascribed to causes similar to those which made it possible for it to maintain its monopolistic position in the manufacture of cigarettes from the domestic leaf. Important among these causes was the possibility of manufacturing little cigars economically by the use of machinery, and the control by the American Tobacco Company of the patented machines.[2]

The development of the Combination's control over the plug tobacco business is shown by the table below:

TOTAL OUTPUT OF PLUG AND TWIST TOBACCO, AND PROPORTION THEREOF MADE BY THE TOBACCO COMBINATION, 1891–1910[3]

Year	*Output.*[4] *000,000 omitted*	*Per cent made by Combination*	*Year*	*Output. 000,000 omitted*	*Per cent made by Combination*
	Pounds			*Pounds*	
1891..	166	2.7	1901..	173	67.7
1892..	171	3.5	1902..	189	71.2
1893..	147	5.9	1903..	186	76.9
1894..	160	5.6	1904..	176	78.2
1895..	167	12.4	1905..	172	80.7
1896..	153	20.1	1906..	182	81.8
1897..	182	20.9	1907..	177	80.5
1898..	165	23.0	1908..	183	81.9
1899..	170	56.3	1909..	192	83.3
1900..	175	62.0	1910..	194	84.9

The total production of plug tobacco has not increased in proportion to the increase in population, but the Combination steadily increased its proportion of the business. In 1891, when the American Tobacco Company by the purchase of the National Tobacco Works entered the plug branch, it produced but 2.7

[1] Report on the Tobacco Industry, part III, p. 181.
[2] Ibid., part I, pp. 31, 345.
[3] Ibid., part III, p. 49.
[4] Includes quantities in bonded warehouses for export.

per cent of the total output. The monopoly of the cigarette trade possessed by it obviously facilitated the expansion of its plug business, since the monopoly profits of the cigarette branch could be used to finance a campaign to push the sale of its plug tobacco. This competitive campaign caused the American Tobacco Company losses exceeding three million dollars for the years 1895 to 1898,[1] but enabled it to increase its percentage by 1898 to 23 per cent of the country's output. The American Tobacco Company thus became the most powerful concern in the trade. Toward the close of 1898 the Continental Tobacco Company was formed; and early in 1899 this company acquired the Liggett and Myers Tobacco Company, and the R. J. Reynolds Tobacco Company (a concern with a very large business in the South). As a result the Combination's proportion was increased to 56.3 per cent in 1899, and to 62.0 per cent in 1900. In almost every year after 1900 the Combination increased its production and its proportion of the total, the percentage having increased by 1910 to 84.9. In almost every year, also, the independent output declined. This decline in the output of the independent concerns, stated the Commissioner of Corporations, speaking of the situation up to 1907, "has been almost wholly due to the transfer of plants from the independent ranks to those of the Combination."[2] A great many of the plants thus acquired were closed, and the brands in many cases were discontinued.

The smoking tobacco branch shows the same general situation. By means already described, the Combination by 1900 had effected control of three-fifths of the smoking tobacco business. Slowly, but surely, after 1900 it increased its hold on the industry, until by 1910 it was producing over three-fourths of the total output of smoking tobacco.[3] After 1900 the independent concerns, despite the purchase of several of their number by the Combination, materially increased their output, but not at so

[1] Report on the Tobacco Industry, part I, p. 367.

[2] Ibid., p. 34. For details see ibid., pp. 364–375.

[3] Ibid., part III, p. 84. Smoking tobacco includes also scrap and cut plug tobacco.

rapid a rate as the Combination,—which was developing not only by internal expansion, but also through outside acquisitions.

The production of fine-cut tobacco is much less than that of plug and smoking tobacco; and it has, moreover, decreased since 1890. The Combination increased its control of fine-cut tobacco from 50.5 per cent in 1900 to 81.7 per cent in 1905; and this percentage was substantially maintained thereafter, the precise figure for 1910 being 79.7 per cent.[1]

As already described, with the organization of the American Snuff Company in 1900 the Tobacco Combination secured control of four-fifths of the country's output of snuff. This control was gradually increased, and by 1910 the trust produced 96.5 per cent of the total output.[2] The growth since 1901 can be explained in part by the absorption of competing concerns, but it was due, in the main, to the increased output of the concerns already owned. The Tobacco Combination's position in the snuff business was more monopolistic in 1910 than in any other branch of the tobacco industry.

In striking contrast, as shown by the table on page 144, stands the cigar industry. The Tobacco Combination for some time previous to 1910 produced only about one-seventh of the cigars made in this country; and was not able to increase this percentage. It had thousands of competitors, many of whom operated on an exceedingly small scale. Unless satisfactory machinery can be invented, and the exclusive patent rights on its manufacture can be obtained by the Combination, this one field of the tobacco industry, in all likelihood, will remain open to independent endeavor.

That the tobacco industry in all the leading branches except cigars was controlled up to the dissolution decree (1911) by a trust or a union of trusts has been shown. By what means was it able to maintain this control?

One thing is clear. The Combination was not able to maintain its position by virtue of the ownership or control of the leaf tobacco,—the most important raw material. The American Tobacco Company controlled, it is true, a few companies pro-

[1] Report on the Tobacco Industry, part III, p. 127. [2] Ibid., p. 138.

TOTAL OUTPUT OF CIGARS, AND PROPORTION THEREOF MADE BY THE TOBACCO COMBINATION, 1898–1910 [1]

Year	*Output. 000,000 omitted*	*Per cent made by Combination*
	Number	
1898.....	4,458	2.2
1899.....	4,909	4.0
1900.....	5,565	4.8
1901.....	6,139	10.9
1902.....	6,231	14.3
1903.....	6,806	16.4
1904.....	6,640	13.9
1905.....	6,747	13.3
1906.....	7,147	14.7
1907.....	7,302	14.5
1908.....	6,488	13.0
1909.....	6,667	13.1
1910.....	6,810	14.4

ducing leaf tobacco in Cuba and Porto Rico, but it did not—nor did any other important manufacturer—engage in the raising of tobacco in the United States.[2] In this respect, therefore, it presents a striking contrast to the steel and oil trusts. The Tobacco Combination endeavored, to be sure, to restrain the operation of the law of supply and demand in the purchase of its leaf tobacco, but it did not obtain nor endeavor to obtain permanent control over the production of the raw material. Clearly there would be little advantage to it in making the attempt, since the large amount of land that might be devoted to tobacco culture would render the failure of the attempt inevitable.

The Tobacco Combination, however, did have a well-nigh complete monopoly of the manufacture of licorice paste in this country. Licorice, next to leaf tobacco, is the most important raw material used in the manufacture of tobacco products. It is used mainly in the manufacture of plug tobacco, but also in the manufacture of smoking tobacco and snuff. The American

[1] Report on the Tobacco Industry, part III, p. 192.

[2] Ibid., part I, p. 48.

Tobacco Company, through the MacAndrews and Forbes Company, produced in 1907, 95 per cent of the total output of licorice paste.[1] The control of the licorice branch served to strengthen greatly the Combination's control of the tobacco industry.

Other important subsidiaries of the American Tobacco Company were the Conley Foil Company and the Johnston Tin Foil and Metal Company, manufacturers of tin foil; the Golden Belt Manufacturing Company, producer of cotton bags to be used in packing tobacco; the Mengel Box Company, manufacturer of wooden boxes; several companies making machinery to be used in tobacco manufacture, or holding patents on machines; the Kentucky Tobacco Product Company, which made nicotine extracts out of tobacco stems, the main by-product of tobacco manufacture; and the Manhattan Briar Pipe Company, manufacturer of pipes and smokers' supplies.[2]

Neither was the Combination's monopolistic position the result of railway rebates,—a factor of so great importance in building up the Standard Oil Company. Because of the fact that tobacco products have generally a large value in small bulk, the item of transportation cuts little figure in the relative position of competing tobacco concerns.

It would undoubtedly be a mistake, furthermore, to attribute the trust to the tariff. The duties on manufactured tobacco products, it is true, have been relatively high, and this has restrained foreign competition. But the imports would hardly be considerable in any event. The United States is the largest producer of leaf tobacco in the world; and though it imports some high grade leaf tobacco, chiefly for cigars, it exports huge quantities. The abundant raw material thus gives to this country a great advantage. The tobacco trust, in fact, is a large exporter of cigarettes; in 1906 about one-third of the total output of cigarettes was exported.[3] The trust's ability to hold the

[1] Brief for the United States in United States v. American Tobacco Company (nos. 118, 119), p. 13.

[2] Report on the Tobacco Industry, part I, p. 24.

[3] Ibid., p. 57.

foreign markets indicates that it would be able successfully to meet foreign competition here. The export, as well as the import, of other tobacco products, however, is insignificant.[1]

When we come to consider the part played by the economies of the trust form of organization, we are on uncertain ground. That the plants of the Combination, generally speaking, were very much larger than those of the independents is certain. This was true of every branch of the tobacco industry. We may take, first, the cigarette branch. In 1906 the tobacco trust manufactured 5,309,000,000 cigarettes, or 82.5 per cent of the country's output. Of this amount, 4,240,000,000, or four-fifths of its output, was produced in three plants, located at New York City, Richmond, Virginia, and Durham, North Carolina.[2] One plant alone—the factory of the British-American Tobacco Company at Durham—made 1,921,000,000 cigarettes, which was over one-third of the trust's output, and almost 30 per cent of the output of the whole country.

This concentration of output was not confined to the factories of the trust. In the same year (1906) there were 528 independent plants (the large number was due to the fact that Turkish cigarettes are often made by hand). Yet six of these plants together produced over three-fifths (61.9 per cent) of the total independent output, or more, therefore, than all the remaining 522 combined.[3] Twelve more yielded 24.6 per cent of the total independent output. This means that 18 of the 528 plants turned out 86.5 per cent of the total output of the independents. Yet in spite of this concentration the independent plants were much smaller than the trust's plants. Two of the trust plants produced more, and one produced almost as much, as all of the independents put together. Whatever advantage might be derived from size belonged, therefore, to the trust. But, of course, the vital question is not, could the trust produce more cheaply than its competitors—that it could do so is hardly to be questioned—but could these big plants of the trust produce more

[1] Report on the Tobacco Industry, part I, p. 57.
[2] Ibid., p. 340.
[3] Ibid.

cheaply by virtue of the fact that they were united under one control. In other words, was the low cost of producing cigarettes by the trust due to the size of its plants or was it due to the union of these plants?

On this point it is difficult to return a definite answer. We may refer, however, to the results of the investigation of the Bureau of Corporations into the comparative costs of the Tobacco Combination and of its successor companies after the enforcement of the dissolution decree.[1] From this investigation it appears that the factory costs of producing cigarettes for the trust were $1.74 per thousand in 1909, and $1.70 per thousand in 1910; while the factory costs for the companies that succeeded the trust were $1.66 per thousand in both 1912 and 1913.[2] The slight reduction in costs effected by the companies when separated from each other was due largely to lower leaf costs in 1912 aud 1913. If we deduct leaf costs, the factory costs were practically the same in each one of these years: 54 cents per thousand in 1909, 55 cents in 1910, 54 cents in 1912, and 52 cents in 1913.[3] This shows, to quote the Bureau, "that so far as manufacturing cost is concerned the question of relative economy relates primarily to the size of the factory units and not to the merger of many factories and companies into a huge consolidation." [4] Or again: "It is evident . . . that the decisive factor in factory costs other than leaf has been volume of output of a particular brand at a single factory and that the status of the organization —that is, whether the factories were in a general consolidation or not—is a subordinate factor." [5] This conclusion of the Bureau, it should be said, did not relate to the cigarette branch alone; it was meant to apply as well to the tobacco business as a whole.

The plug plants of the trust were also distinctly larger than those of the independent concerns. In 1906 the trust had 8 plug plants with an output of 5,000,000 pounds or more each.[6] These plants turned out 91.4 per cent of its total production of plug. Yet two of these eight plants produced 59.4 per cent of the

[1] On the dissolution proceedings, see ch. 18.
[2] Report on the Tobacco Industry, part III, p. 324.
[3] Ibid., p. 326.
[4] Ibid., p. 15.
[5] Ibid., p. 16.
[6] Ibid., part I, p. 376.

trust's output, and 48.7 per cent of the country's output. The independents, on the other hand, had no plants as large as any of these eight; the larger independents had all been acquired by the trust. Forty-two and a half per cent of the independent production was produced in the seven plants having an output of 1,000,000 pounds or more, and 50.8 per cent in the forty-four plants producing between 100,000 pounds and 1,000,000 pounds. The balance (6.7 per cent) was produced in the remaining plants, 129 in number.

The aforementioned investigation of the Bureau of Corporations shows for the plug business that the factory costs of the companies that succeeded the trust upon its dissolution were less than the costs of the trust itself. These factory costs were as follows: 20.0 cents per pound in 1909; 19.5 cents in 1910; 18.1 cents in 1912; and 18.5 cents in 1913.[1] But the leaf costs of the successor companies were distinctly less in 1912 and 1913 than those of the trust in 1909 and 1910; and this explains all the decline in factory costs. In fact, if we deduct leaf costs, the factory costs of the successor companies were actually greater, yet by a very small fraction. It seems to be clear, therefore, that so far as factory costs were concerned, it was not the trust itself that was principally responsible for the low production costs; it was rather the tremendous size of its plants.

What has been said of the cigarette and plug branches applies substantially to the others,[2] though especial mention may be made of the cigar branch.

With respect to cigars, the Tobacco Combination in 1906 had two plants making over 50,000,000 cigars, the average output of these two plants for that year being about 190,000,000.[3] There were no independent plants producing as many as 50,000,000 cigars; hence the Combination had easily the two largest plants. Over one-third of its output, in fact, was produced in these two

[1] Report on the Tobacco Industry, part III, p. 224.

[2] On smoking tobacco see Report on the Tobacco Industry, part I, pp. 391–396, part II, pp. 251–256; on snuff see part I, pp. 402–406, part II, pp. 307–312.

[3] Report on the Tobacco Industry, part I, p. 425.

plants. But these plants produced largely cheroots and small cigars, rather than the ordinary domestic cigars. When we turn to the remaining cigar plants of the Combination—44 in number—we find that they were of widely varying sizes; and that many of them were much smaller than a number of the independent plants. It is true that the average output of the Combination's cigar plants exceeded by many times the average output of the independent factories, but in considerable measure this was due to the existence of some 25,000 cigar factories turning out a very small output. Except for its two largest factories, the Combination had no great advantage with respect to size over its larger competitors. Were size as important as for the other branches, the Combination would doubtless have acquired its leading competitors, and thus have strengthened its position in this respect. But size was not vital in this branch, and for this reason apparently the Combination was not able to establish monopoly control. The mere possession of 80 to 90 per cent of the cigar manufacture would not enable it to fix monopoly prices for any length of time; the increase of independent production would be certain, and with it monopoly control would be lost.

The report of the Bureau on costs does not take up the cigar branch, and for this reason a comparison can not be made of the costs of the cigar plants of the Combination before and after the dissolution.

The foregoing discussion indicates that the size of the plant is the determining factor in the cost of production, and that the dissolution proceedings, since they left the big plants intact, did not affect materially the factory costs. But the situation is otherwise as to selling costs. The subdivision of the business provided for in the dissolution decree led to a duplication of selling organization and an increased overhead expense; and the result was a general increase in selling costs. Thus, the selling costs of the trust in all branches except cigars amounted in 1910 to $7,191,676, while in 1913 the selling costs of the companies that succeeded to its business amounted in the same branches to $9,818,746, an increase of over two and a half million dollars.[1]

[1] Report on the Tobacco Industry, part III, p. 17.

In every branch, except flat plug and Turkish cigarettes, the selling costs showed an increase. Based on the rates per thousand or per pound, the selling costs of the successor companies in 1913 in the cigarette branch were 55 per cent greater than for the trust in 1910; 91 per cent greater in the little cigar branch; 11 per cent greater in navy plug; 39 per cent greater in plug-cut smoking; 40 per cent greater in granulated smoking; 44 per cent greater in fine-cut chewing; and 46 per cent greater in snuff. The selling costs of the successor companies for flat plug and Turkish cigarettes, on the other hand, were only 76 and 83 per cent, respectively, of the costs of the trust in these branches.

The advertising expenditures of the successor companies also greatly increased as compared with the expenses of the trust. The advertising expenses of the trust in 1910 in all branches except cigars were $10,895,132, while those of the successor companies in 1913 amounted to $23,623,564, or more than double.[1]

The trust may likewise have effected some economies in the purchase of its supplies. While the American Tobacco Company manufactured many of the articles that it needed in its business, including packages, boxes, etc., it had occasion to buy large supplies, such as sugar, rum, flavoring extracts, stationery, machinery, tools, and furniture. All of its buying, as well as that of its affiliated companies, such as the American Snuff Company and the American Cigar Company, was done for it by one concern,—the Amsterdam Supply Company.[2] By buying through one company with its experienced purchasing agents, the trust was possibly able to get some of its supplies on more advantageous terms.

The trust also found the control of patented machinery a source of great strength. The concentration of the manufacture of tobacco in large plants and the specialization of these plants, to a large degree, on particular brands, permitted a wider utilization of machine methods than was possible for smaller concerns. The trust substituted machinery for hand labor

[1] Report on the Tobacco Industry, part III, p. 18.

[2] Ibid., part I, p. 265.

whenever practicable, and it achieved its greatest success in those lines in which this was done. In the cigarette and little cigar branches, where practically all the processes were performed by machinery, the trust, through its control of the patented machines, was able to maintain a monopoly position more easily than in any other branch of the tobacco industry except snuff. In the cigar branch, where machinery is least used, and where patents therefore give no advantage, the trust has been weakest.

The trust, as shown earlier, also made frequent use of the practice of local price discrimination,—the weapon so effectively employed by the Standard Oil Company. In the localities where independents sought a foothold, the trust frequently sold its so-called "fighting brands" at a loss; and in this way checked the growth of the independent concerns, whose field of competition was generally local. This proved especially effective, because the campaign of competition could be limited to the comparatively few fighting brands held by the trust, the prices of its popular brands being generally maintained at the former level. The practice of local price cutting touched as a rule, therefore, only the fringes of the trust's vast business, but commonly affected the total business of the independents, and this made it more difficult for them to bear the losses of such a campaign.

The policy of local price cutting was facilitated through the secret ownership of a number of tobacco companies. Many dealers and consumers had long been opposed to trusts in general and to the tobacco trust in particular. To take advantage of this attitude independent manufacturers frequently advertised their goods as "not made by a trust." The refusal of the trust to deal with labor organizations had engendered much hostility among the trade unionists also, and many of them refused to buy any but union made goods. Manufacturers catering to this sentiment were able to develop quite a trade. In order to meet this situation, the trust, especially during 1903 and 1904, secretly secured a controlling interest in a number of concerns catering to the anti-trust and pro-union trade. These concerns, after being acquired by the trust, continued to operate under their former management, and pretended to be independent and op-

posed to the trust.[1] Those which had friendly relations with union labor continued to maintain such relations, though the attitude of the trust itself was one of bitter hostility to trade unionism. These secretly controlled concerns were, until the facts became known, a highly effective engine of warfare against the real independents.[2]

The American Tobacco Company likewise endeavored to control the jobbing trade. In the cigarette business, for example, a factor's agreement, or a consignment agreement as it was called, was put in operation in the latter part of 1895.[3] According to this agreement the jobber to whom cigarettes were consigned agreed to sell only to the retail trade, and to sell only at the price fixed by the American Tobacco Company. If the jobber did not discriminate against the American Tobacco Company's cigarettes, and fully complied with all the provisions of the agreement, he was to be given a commission of 2½ per cent on the receipts of his sales of cigarettes. If, however, the jobber handled no cigarettes except those of the American Tobacco Company (and complied in every respect with the consignment agreement), he was to receive an additional commission of 7½ per cent. Mr. Whelan, a wholesale dealer, claimed before the Lexow Committee (1897) that a jobber could hardly do business without some of the goods of the American Tobacco Company; that 2½ per cent allowed the dealer no profit; and that there was, therefore, a very strong incentive to agree to handle the American Tobacco Company's goods exclusively.[4] This device for holding the trade led to adverse legislation, and in 1897 was abandoned.

The ability of the trust to require preference in the sale of its goods,—to the extent that it possessed such ability,—lay in considerable measure in its exclusive ownership of a great majority

[1] Report of the Tobacco Industry, part I, p. 224.

[2] For excellent illustrations of the secret machinations of the trust, see Transcript of Record in United States *v.* American Tobacco Company (no. 660), vol. II, pp. 524, 640; and Report of the Senate Committee on Control of Corporations, 1913, p. 347.

[3] Lexow Report, p. 872. A copy of the agreement is in Lexow Report, pp. 878–883.

[4] Ibid., pp. 991–992.

of the popular brands of tobacco products. Some of these brands had became such standard articles that dealers had to handle them, or lose a great deal of business even in other lines. In fact, the trust's monopoly power was to a large extent founded on its control of the greater number of the brands enjoying a high degree of popular favor.

The tobacco trust also undertook the retail distribution of its products. This it did largely through the acquisition of the United Cigar Stores Company. This concern had been incorporated in New Jersey on May 16, 1901, by persons having no connection with the trust, to sell and distribute tobacco products at retail.[1] The company proved so successful that the American Tobacco Company acquired a controlling interest in it in November, 1901; and thereafter it supplied it with the necessary funds for expansion.[2] The United Cigar Stores Company bought its products direct from the American Tobacco Company and the American Cigar Company, instead of through jobbers, but it handled the goods of independents also. In 1907 the United Company had 392 stores, but subsequently the number was much increased.

It is thus clear that a great many factors contributed to the success of the tobacco trust in establishing and maintaining its monopolistic position. The great size of its plants, the control of the licorice paste, tariff protection, the ownership of patents on machinery used in tobacco manufacture, the use of local price discrimination and bogus independent concerns, numerous devices to control the wholesale and retail distribution of its product,—all helped it in the competitive struggle. Yet the growth of the trust's control of the tobacco industry, according to the Commissioner of Corporations, "has been primarily due to continual buying up of independent concerns."[3] Frequent instances of such purchases have already been given. Their influ-

[1] Report on the Tobacco Industry, part I, p. 88.

[2] Brief for the United States in United States *v.* American Tobacco Company (nos. 118, 119), p. 12. On December 31, 1906, the American Tobacco Company held $340,000 of the $450,000 common stock of this company, and all of its bonds and preferred stock.

[3] Report on the Tobacco Industry, part I, p. 38.

ence is further shown by a comparison of the number of factories, with their output, owned at different periods by the trust with the number owned by the independents. The years 1897, 1900, and 1906 are significant years. From a table given in the report of the Bureau of Corporations it appears that in 1897 the trust owned five plants producing chewing and smoking tobacco and snuff with an output of five million pounds each, while the independent concerns had seven plants of this size.[1] In 1900 the independents had only one such plant, all of the remaining six having been acquired by the trust, which in that year was operating ten plants producing as much as five million pounds each. By 1906 the seventh independent plant had been acquired by the trust, and the trust had increased the output of some of its smaller plants, so that it had twenty-one factories all told of the size mentioned. There were only two independent concerns producing over five million pounds in 1906, two new concerns having arisen with an output of this amount. To quote from the report of the Bureau, "despite enormous expenditures for advertising and in 'schemes' and despite frequent price cutting by means of its so-called 'fighting brands' and its bogus independent concerns, there has been, in several branches of the industry, a constant tendency for competitors to gain business more rapidly than the Combination and thus to reduce its proportion of the output. This tendency has been overcome only by continued buying up of competitive concerns. Many weaker concerns have been virtually driven out of business or forced to sell out to the Combination, either by reason of the direct competition of the latter, or as an indirect result of the vigorous competition between the Combination and larger independent concerns. In the case of the larger and more powerful concerns which it acquired, however, the Combination has usually secured control only by paying a high price. The immense profits of the Combination have enabled it to keep up this policy." [2]

What effect has the trust had upon the prices of tobacco products? We may take up first the cigarette branch. The American Tobacco Company (the cigarette trust) was organized in

[1] Report on the Tobacco Industry, part I, p. 39. [2] Ibid., p. 41.

1890. In what way the establishment of this trust affected prices can not be said; the detailed data with respect to the years immediately following the formation of the company are not obtainable. The really significant figures, therefore, are lacking. The prices from 1893 to 1910, however, are available, and these are shown in the following table. The prices are wholesale, since the trust sold largely to jobbers.

WHOLESALE PRICES OF CIGARETTES RECEIVED BY THE TRUST ON ITS DOMESTIC BUSINESS, 1893–1910 [1]

Year	*Number sold. 000,000 omitted*	*Average per thousand*				
		Net price	*Tax*	*Net price less tax*	*Cost* [2]	*Profit*
1893.....	2,588	$3.52	$0.50	$3.02	$1.74	$1.28
1894.....	2,601	3.49	.50	2.99	1.63	1.36
1895.....	2,919	3.27	.50	2.77	1.56	1.21
1896.....	3,094	2.96	.50	2.46	1.40	1.06
1897.....	2,883	2.94	.67	2.27	1.27	1.00
1898.....	2,564	3.27	1.25	2.02	.97	1.05
1899.....	2,495	3.51	1.50	2.01	.89	1.12
1900.....	2,241	3.66	1.50	2.16	1.00	1.16
1901.....	1,990	3.61	1.27	2.34	1.31	1.03
1902.....	2,040	3.86	1.01	2.85	2.04	.81
1903.....	2,402	4.05	1.01	3.04	2.01	1.03
1904.....	2,433	4.00	1.00	3.00	2.04	.96
1905.....	2,686	4.09	1.00	3.09	2.02	1.07
1906.....	3,211	4.26	1.01	3.25	2.19	1.06
1907.....	3,859	4.24	1.02	3.22	2.30	.92
1908.....	4,376	4.42	1.02	3.40	2.35	1.05
1909.....	5,362	4.49	1.02	3.47	2.37	1.10
1910.....	6,930	4.66	1.15	3.51	2.51	1.00

The net price less tax on all the cigarette business of the trust, exclusive of exports and foreign output, averaged $3.02 per thousand in 1893. From then until 1899 it steadily declined, reaching $2.01 in 1899. This proved to be the low point. Thereafter until 1910 the price increased almost continuously, and in that year reached $3.51. But the increase in prices since 1893 or

[1] Report on the Tobacco Industry, part III, p. 155.

[2] Includes manufacturing, selling, advertising, and freight.

even since 1899 (the low point) has not been commensurate with the increase in the cost of production; and the profit in 1910 was less, therefore, than in either 1893 or 1899. It is difficult to say just what significance attaches to these figures. The important thing, clearly, would be a comparison of the range of prices for cigarettes after the trust was established in 1890 with the range prior to that time. Data on this point being lacking, a comparison might be made of the prices charged for tobacco before and after the dissolution of 1911. Yet for reasons given on page 472 such a comparison would not lead to any definite conclusions.

No conclusions of especial value can be drawn from a study of the prices of little cigars. Until 1898 cigarettes and little cigars were grouped together in reports made to the Bureau of Internal Revenue, and therefore it is not possible to say what proportion of the little cigar business was controlled up to that time by the trust. In 1898 (when the statistics were first separated) the trust produced 48.7 per cent of the little cigars, and its control gradually increased until in 1910 it was as high as 91.4 per cent. The net price less tax, as the table on page 182 of the report of the Commissioner of Corporations on Prices shows, was distinctly less in 1910 than in 1895 (the first year for which these statistics are available [1]), and was no higher than in 1898 when the Combination controlled only half the little cigar industry. But the cost meanwhile had declined greatly. The cost in 1910 was 64 cents less per thousand than in 1898, and the price about the same as in 1898. It follows that the profit was very much larger,—in fact, it was more than double. It appears, therefore, that the trust was able to maintain prices; that it prevented the reduction in prices which under competitive conditions might be expected to follow a considerable decline in the cost of production. To arrive at any definite conclusions, however, we should know what prices and costs would have been had there never been a little cigar trust, and that of course can not be ascertained.

The statistics for plug tobacco are perhaps more significant.

[1] The American Tobacco Company kept the statistics for its little cigar business separately as early as 1895. Report on the Tobacco Industry, part III, p. 182.

One reason is that they are obtainable since 1893, or several years before the formation of the plug trust. This renders it possible, therefore, to make a comparison which could not be made for the cigarette and little cigar branches,—a comparison of the prices immediately before and after the organization of the trust. The plug trust (the Continental Tobacco Company) controlled 56.3 per cent of the business in 1899, and gradually increased this control to 81.8 per cent in 1906. The relation between steadily increasing monopolistic control and prices can thus also be pointed out.

The essential figures are shown in the following table:

WHOLESALE PRICES OF PLUG TOBACCO RECEIVED BY THE TRUST, 1893–1910 [1]

Year	*Pounds sold. 00,000 omitted*	*Average per pound*				
		Net price	*Tax*	*Net price less tax*	*Cost* [2]	*Profit*
		Cents	*Cents*	*Cents*	*Cents*	*Cents*
1893.....	8.3	34.0	6.0	28.0	30.6	[3] 2.6
1894.....	8.8	35.1	6.0	29.1	27.9	1.2
1895.....	20.3	21.5	6.0	15.5	20.0	[3] 4.5
1896.....	31.1	18.9	6.0	12.9	17.3	[3] 4.4
1897.....	37.8	18.2	6.0	12.2	14.6	[3] 2.4
1898.....	32.9	25.2	8.5	16.7	19.6	[3] 2.9
1899.....	85.9	33.0	12.0	21.0	18.8	2.2
1900.....	110.8	34.8	12.0	22.8	19.0	3.8
1901.....	118.0	36.0	10.9	25.1	18.6	6.5
1902.....	132.6	35.5	7.8	27.7	19.3	8.4
1903.....	132.2	35.4	6.0	29.4	19.6	9.8
1904.....	124.2	35.9	6.0	29.9	22.1	7.8
1905.....	132.9	36.2	6.0	30.2	22.4	7.8
1906.....	138.2	36.0	6.0	30.0	21.1	8.9
1907.....	137.8	36.2	6.0	30.2	21.8	8.4
1908.....	147.2	36.3	6.0	30.3	22.3	8.0
1909.....	156.9	35.7	6.0	29.7	24.6	5.1
1910....	154.6	36.0	6.9	29.1	24.4	4.7

[1] Report on the Tobacco Industry, part III, p. 51.

[2] Includes manufacturing, selling, advertising, and freight.

[3] Loss.

In 1894, when there was no important concentration of the plug business in the hands of any one concern, the net price less tax averaged 29.1 cents per pound. The inauguration by the American Tobacco Company of its campaign for the plug business led to severe cuts in prices. The existence and severity of this competition is shown by the figures for 1895 to 1898. The average price per pound fell from 29.1 cents in 1894 to 15.5 cents in 1895, to 12.9 cents in 1896, and to 12.2 cents in 1897. In the spring of 1898 an agreement looking toward consolidation was reached, and largely as a result the average price for 1898 rose to 16.7 cents per pound,—quite a bit higher than in 1897. In 1899, the year of the acquisition of the Liggett and Myers concern, the price rose to 21.0 cents, and in 1900 to 22.8 cents. As the trust increased its control year by year the price rose, and with it the profit. By 1901 the price had advanced to 25.1 cents, or more than double the price of 1897; and the profit was 6.5 cents per pound as compared with a loss of 2.4 cents in 1897. By 1908 the high-water mark in prices was reached at 30.3 cents, the profit in that year being 8.0 cents per pound. The Continental Tobacco Company at this time controlled 81.9 per cent of the business. The year 1908 was not the year of maximum profit, however, because the cost was higher than in 1903, when a profit of 9.8 cents per pound was attained.

The power and influence of the trust is indicated, though not proven, by the course of prices during the years 1901 to 1903. The internal revenue tax on plug tobacco had been 12.0 cents per pound in 1900. In 1901 it was reduced to 10.9 cents, in 1902 to 7.8 cents, and in 1903 to 6.0 cents. In spite of these marked tax reductions, the net price (including tax) rose from 34.8 cents in 1900 to 36.0 cents in 1901, and by 1903 had declined to only 35.4 cents. In other words, during a period when the tax was reduced by 6 cents, presumably in the interests of the consumer, the price actually increased six-tenths of one cent. The cost of production during these years increased by exactly the same amount as the price. It is evident, therefore, that the consumer got no benefit from the reduction in the tax; and that he was forced to pay six-tenths of a cent more to compensate the trust

for the increase in costs,—an increase which exactly equalled the rise in price. In view of these facts, the profits of the trust must have greatly increased. The profit per pound had been 3.8 cents in 1900; in 1903 it was 9.8 cents, or over 150 per cent greater.

The remission of the internal revenue taxes on the other tobacco products during 1901 and 1902 had substantially the same result; the trust absorbed the gains (or practically all of them) that were presumably intended for the consumers of tobacco.

In 1910 the reverse situation appeared in part. In that year the internal revenue tax was increased somewhat all along the line, and this added burden was largely borne by the trust. While in the smoking and fine-cut branches prices were advanced, these increases being passed along by the jobber to the consumer, in the cigarette, little cigar, plug, and snuff branches, the trust advanced its price to the jobber but slightly, and the jobber absorbed the increase, leaving the price to the consumer unchanged.[1] The trust might have reduced the quantities of these products in the retail packages, as it did in the smoking tobacco and fine-cut branches, but this would generally have doubled the profits,—a step that did not seem advisable, especially in view of the pending dissolution suit.

Similar price statistics are available for smoking tobacco, snuff, and cigars. However, it would burden the record unduly to insert them here. Yet a comparison of the snuff and cigar businesses with respect to their profits is of great significance. Of all the branches of the tobacco industry, the snuff branch is the most highly monopolized, while the cigar branch is the only one the trust has been unable to dominate. The table on page 160 shows for the trust in these two lines the percentage of the price which represented profits (not the profit per pound or per thousand).[2]

During the years 1901–1910, from 54.1 per cent to 73.7 per cent of the price of snuff stood for cost, and from 45.9 per cent to 26.3 per cent represented profit. For cigars (leaving out of con-

[1] Report on the Tobacco Industry, part III, p. 7.

[2] Ibid., pp. 142, 199.

RATE OF PROFIT (PERCENTAGE THAT PROFIT WAS OF THE PRICE) ON SNUFF AND DOMESTIC CIGARS, 1900–1910

Year	*Snuff*	*Domestic cigars* [1]
1900.....	18.2	
1901.....	26.3	0.6 [2]
1902.....	33.7	22.5 [2]
1903.....	37.1	11.2 [2]
1904.....	41.5	4.4 [2]
1905.....	41.8	6.0
1906.....	45.9	10.7
1907.....	44.0	10.0
1908.....	43.7	3.9
1909.....	43.8	8.6
1910.....	44.9	5.8

sideration the years 1901–1904, when the tobacco trust was trying to capture the cigar business) the cost of manufacture ranged from 89.3 per cent to 96.1 per cent of the price, and the profit, therefore, ranged from 3.9 per cent to 10.7 per cent of the price. If we take the year 1906 (when the profits in the cigar branch were greatest), it appears that the rate of profit in the highly monopolized snuff business exceeded the rate of profit in the competitive cigar industry by well over four times. A similar comparison made for the other branches would show that the trust's rate of profit in the cigarette, plug, smoking tobacco, and little cigar business exceeded its rate of profit in the domestic cigar business by three, three, two and a half, and two times, respectively.[3] It is also significant that the cigar branch was the only one in which the price, either with or without tax, showed a declining tendency during the ten years ending in 1910. The net price less tax on the trust's domestic cigars averaged $27.83 per thousand in 1901, and only $24.50 in 1910. The bearing of these figures on the general question of monopoly versus competition is obvious.

[1] Excludes stogies, cheroots, and package cigars.

[2] Loss.

[3] Report on the Tobacco Industry, part III, p. 200.

The price tables presented above are for wholesale prices,—the prices paid by jobbers. The prices paid by consumers during this period did not increase in anything like the same proportion; in fact, during the period from 1901 to July, 1910, there were practically no changes in the retail prices of the trust's principal brands of cigarettes, little cigars, and manufactured tobacco.[1] It follows, therefore, that during this period the trust was gradually encroaching upon the margin between the jobber's and the consumer's price. In part this may be explained by the trust's policy of performing itself to a large extent the function of pushing the sale of its goods (thus reducing the jobbers' expenses and making it possible for them to get along on a lower margin). In part also it testified to the great power of the trust.

We turn next to an analysis of the profits of the tobacco trust. The table on page 162 shows for the American Tobacco Company the earnings and dividends on the common stock for the years 1890 to 1903 (in 1904 the American Tobacco Company and the Continental Tobacco Company were merged).

The earnings of the American Tobacco Company have been handsome, and especially in the early years. The average for the nine years 1890 to 1898, embracing a period of severe industrial depression, was 17.7 per cent, not counting the profits realized from the sale of the plug business to the Continental Tobacco Company. If these are included, the earnings averaged as high as 25.7 per cent.[2] The declaration of a 100 per cent stock dividend in 1899 naturally reduced the rate of earnings, yet in spite of this dilution of the stock as much as 13.8 per cent was earned in 1903.

The dividends paid were also liberal. In the fourteen years prior to the merger, the dividends declared on the common stock, including stock dividends and scrip, averaged about 15 per cent per annum. This common stock was largely water. At its organization in 1890 the American Tobacco Company had issued $10,000,000 preferred stock and $15,000,000 common. According to the Bureau of Corporations, the tangible assets of the five com-

[1] Report on the Tobacco Industry, part III, p. 7.

[2] Ibid., part II, p. 58.

EARNINGS AND DIVIDENDS OF AMERICAN TOBACCO COMPANY ON ITS COMMON STOCK, 1890–1903 [1]

Year	Common stock	Profits available for distribution on common stock after paying dividends on preferred stock and interest on scrip		Rate of dividend paid on common stock
		Amount	Per cent	
1890	$15,000,000	$1,711,180	11.4	10.0
1891	17,900,000	3,441,994	19.2	12.0
1892	17,900,000	3,760,501	21.0	12.0
1893	17,900,000	3,373,167	18.8	12.0
1894	17,900,000	4,114,615	23.0	12.0
1895	17,900,000	2,911,693	16.3	9.0
1896	17,900,000	2,475,176	13.8	29.0 [3]
1897	17,900,000	2,995,300	16.7	8.0
1898	21,000,000	3,735,983	17.8 [2]	8.0
1899	54,500,000	3,890,240	7.1	106.5 [4]
1900	54,500,000	5,002,663	9.2	6.0
1901	54,500,000	5,346,224	9.8	6.0
1902	54,500,000	6,270,291	11.5	10.0
1903	54,500,000	7,544,784	13.8	12.0

panies which united to form the trust aggregated $3,545,108, and the good will (which was recognized as a legitimate factor in the investment, because it had generally been built up by large expenditures for advertising, etc.) certainly did not exceed $8,954,892.[5] As a very liberal estimate the value of the business (allowing for the $1,825,354 in notes given by the organizers) was only $14,325,000, and property of this amount was represented by $10,000,000 of 8 per cent preferred stock and by $15,000,000 of common

[1] Original Petition in United States *v.* American Tobacco Company, pp. 78–84, and Report on the Tobacco Industry, part II, p. 57.

[2] Does not include the profits received from the sale of the plug business.

[3] 9 per cent paid in cash; 20 per cent in scrip, afterward redeemed at its face value, with interest at 6 per cent from May 1, 1896.

[4] Includes 100 per cent stock dividend.

[5] Report on the Tobacco Industry, part II, pp. 8–9.

stock. Over two-thirds of the common, therefore, was water. Thus, the American Tobacco Company, though paying 10 per cent dividends in 1890, was actually paying at least 34 per cent on the value of that part of its property which stood back of the common stock. The fact that it was able from the very start to pay excellent dividends on its whole capitalization indicates that a high degree of monopolistic control had been effected.

Similar data might be presented in detail for the Continental Tobacco Company from 1899 to 1903; for the Consolidated Tobacco Company from 1901 to 1904; and for the reorganized American Tobacco Company from 1904 to 1908. It will suffice to point out that even on the capitalization basis the earnings of these companies and the dividends paid were very liberal. The reorganized American Tobacco Company, for example, earned on its common stock during the years 1905 to 1910 an average of over 50 per cent; and paid dividends averaging over 29 per cent.[1]

The foregoing statistics give a fairly satisfactory idea of the profits of the trust. But for two reasons they do not portray the situation accurately. In the first place, the capitalization was an arbitrary figure; and, in the second place, the earnings were not the actual earnings, but merely those shown on the companies' books. The Bureau of Corporations therefore attempted in its elaborate investigation of the profits of the tobacco business to ascertain as accurately as it could the investment and the actual earnings,—that is, to determine what the money invested in the tobacco manufacture had really earned. Space is not available to present the results of this study;[2] it must suffice to say that after 1901, by which date effective control had been secured over practically all branches of the tobacco industry, the earnings of the tobacco trust on its entire business closely approximated the large profits obtained by the American Tobacco Company during the earlier period when it almost completely monopolized the cigarette business.

[1] Moody's Manual, 1911, p. 2696. No dividends were paid in 1904, the year in which the American Tobacco Company was organized.

[2] The interested reader is referred to Report on the Tobacco Industry, part II (Capitalization, Investment, and Earnings).

CHAPTER VIII

THE UNITED SHOE MACHINERY COMPANY[1]

Practically all of the shoes now made in this country are manufactured by machinery. In 1915 there were over 1,500 manufacturers of shoes scattered throughout the country, producing annually in the aggregate more than 300,000,000 pairs of machine-made shoes. A very important group of these machines is that used to prepare and attach the soles to the uppers,—a process known in the trade as bottoming. The more important of the bottoming machines, without which factory shoes can not profitably be made, are the lasting machines, the welt-sewing machines, the outsole-stitching machines, the heeling machines, and the metallic-fastening machines.[2] By the year 1899, through a process of combination, there had developed a dominating concern in the manufacture of each one of these groups of machines. The Consolidated and McKay Lasting Machine Company under letters patent manufactured 60 per cent of the lasting machines made in this country; the Goodyear Shoe Machinery Company produced 80 per cent of the outsole-stitching machines, and 10 per cent of the lasting machines; and the McKay Shoe Machinery Company made 70 per cent of the heeling machines, and 80 per cent of the metallic-fastening machines.[3]

[1] On the United Shoe Machinery Company see: Original Petition in United States *v.* United Shoe Machinery Company in the district court of the United States for the eastern district of Missouri; Brief for the United States in United States *v.* United Shoe Machinery Company (no. 207); 227 U. S. 202–218; 222 Fed. Rep. 349–415; 247 U. S. 32–91; 264 Fed. Rep. 138–175; Report of the Senate Committee on Interstate Commerce on the Control of Corporations, 1913; Hearings on Trust Legislation held before the House Committee on the Judiciary, 1913–1914; Roe, Journal of Political Economy, 21, pp. 938–953, and 22, pp. 43–63.

[2] For a description of these machines and of the process of shoe manufacture, see Brief for the United States (no. 207), pp. 7–15.

[3] See 227 U. S. 215. Mr. Winslow, president of the United Shoe Machin-

The heads of the Consolidated Company and the Goodyear Company in negotiations begun in 1898 discussed a "working agreement" between the two companies, but this proposed arrangement was given up because of the objections of the head of the Goodyear Company. This gentleman, who was a lawyer, "had a sort of indefinite idea that it might be deemed to be a combination in restraint of trade," and he therefore insisted upon a complete consolidation, the illegality of which (as a device for organizing trusts) was less certain at that time.[1]

Accordingly on February 7, 1899, the United Shoe Machinery Company was incorporated in New Jersey with an authorized capital stock of $25,000,000. The new company acquired all the stock of the three concerns mentioned above, as well as four other concerns, to wit, the International Goodyear Shoe Machinery Company, the Davey Pegging Machine Company, the Eppler Welt Machine Company, and the International Eppler Welt Machine Company.[2] These companies conveyed to the United Company all of their business, including their patent rights in the United States and foreign countries.[3] The United Company thus became an operating concern. It soon concentrated the manufacture of its machines at a new plant in Beverly, Massachusetts; and here the greater number of its machines are now made. The effect of the combination of 1899, according to counsel for the government, was to give one concern control over 70 to 80 per cent of the total output of bottoming room machinery (the company, it should be noted, did not secure control of the machinery used in the sole leather room, the stitching room, or the finishing room).[4] After its organization the United Company acquired some fifty other concerns manufacturing shoe machinery or supplies.[5] As the result of the original combination and subsequent acquisitions the United Company obtained a complete line of the principal and auxiliary

ery Company, testified that the McKay Shoe Machinery Company produced nearly all of the heeling and metallic-fastening machines that were being made in the United States. 247 U. S. 81.

[1] 247 U. S. 77.
[2] Ibid., 38–39.
[3] Ibid., 39.
[4] 227 U. S. 205.
[5] Brief for the United States (no. 207), p. 67.

machines used in the bottoming of shoes. Formerly, as stated above, certain companies had held a monopolistic position with respect to individual bottoming room machines, but no one had a full line, and no one has a full line at the present time, except the United Shoe Machinery Company.[1]

Not only is the United Company the only American concern possessing a full line, but it has a highly monopolistic position in the manufacture of the leading bottoming room machines,—and it is with respect to bottoming room machinery that the controversy of the government with the United Company deals. In the Brief for the United States there is an exhibit that shows the number of principal bottoming machines (together with clicking machines) which the United Company and its competitors had out on March 1, 1911.[2] This exhibit is reproduced below, the percentages being supplied by the author.

MACHINES PUT OUT TO SHOE MANUFACTURERS IN THE UNITED STATES, MARCH 1, 1911

Machines	*By defendants*	*By all others*	*Per cent of competition*
Clicking machines	3,655	none	0.00
Pulling-over machines	1,632	none	0.00
Lasting machines [3]	7,496	7	0.01
Standard screw machines [3]	409	none	0.00
Pegging machines [3]	146	none	0.00
Tacking machines [3]	3,488	6	0.02
Welt-sewing machines [3]	2,527	142	5.30
Outsole-stitching machines [3]	2,676	758	22.07
Loose-nailing machines [3]	1,835	24	1.30
Heeling machines [3]	2,019	17	0.83
Slugging machines	1,876	23	1.21
McKay sewing machines	898	8	0.87
	28,657	985	3.44

[1] Brief for the United States (no. 207), p. 134.

[2] This table was constructed from the uncontradicted evidence of eighty-five witnesses, from an exhibit of the United Company, and from other sources. See Brief for the United States (no. 207), p. 150.

[3] The figures for these machines are reproduced in the opinion of Justice Clarke (247 U. S. 89), who states that they are not seriously disputed by counsel for the United Shoe Machinery Company.

From this table it appears that in only one bottoming room machine—the outsole-stitching machine—did the United Shoe Machinery Company have important competition. The independent companies made (1911) 22.07 per cent of the outsole-stitching machines; and the United Company made 77.93 per cent. Of every other machine the United Company made at least 94 per cent, and in some cases 100 per cent. Taking all these machines together the trust made 96.56. per cent. The petition of the government even charged that the United Company made 98½ per cent of the machinery and supplies used in the bottoming of shoes.[1]

In addition the shoe machinery trust had a very strong hold on the business of foreign countries.[2] The British United Shoe Machinery Company supplied all of the installed shoe machinery equipment in Ireland, practically all in Scotland, and some 80 per cent in England. Other affiliated companies furnished 90 per cent of the shoe machinery equipment of Italian factories, and 75 per cent of that of French factories. United machines were sold also in Germany, Austria, Belgium, Russia, Denmark, Norway, Sweden, Spain, Switzerland, and undoubtedly other countries.

To what may be the ability of the United Shoe Machinery Company to attain a monopolistic position in the industry be attributed? It can not be ascribed to tariff barriers. There have been duties on the importation of shoe machinery (though none since 1913), yet the ability of the United Company to compete so effectively in foreign lands shows conclusively that its strong position at home is not to be explained in this way. Neither does it appear to have benefited by railway favors. Furthermore, no monopoly of a natural resource has been effected. To what, then, may it be attributed?

In the first place, the strength of the shoe machinery trust was due to the original act of combination in 1899. The mere

[1] Original Petition in United States *v.* United Shoe Machinery Company, pp. 15–16.

[2] See the Shoe and Leather Trade series of the Department of Commerce and Labor, 1912–1913.

union under one management of a group of concerns, each of which had a dominant position in its special line of bottoming room machinery, gave the United Company a substantial monopoly of all such machinery. A vital question is the proper public policy to be adopted with respect to such combinations. In this connection the remarks of the Supreme Court are of interest. Speaking of the organization of the United Shoe Machinery Company in 1899 it said: "On the face of it the combination was simply an effort after greater efficiency. The business of the several groups that combined, as it existed before the combination, is assumed to have been legal. The machines are patented, making them a monopoly in any case . . . and it may be assumed that the success of the several groups was due to their patents having been the best. As, by the interpretation of the indictment below, 195 Fed. Rep. 591, and by the admission in argument before us, they did not compete with one another, it is hard to see why the collective business should be any worse than its component parts.[1] It is said that from seventy to eighty per cent. of all the shoe machinery business was put into a single hand. This is inaccurate, since the machines in question are not alleged to be types of all the machines used in making shoes, and since the defendants' share in commerce among the States does not appear. But taking it as true we can see no greater objection to one corporation manufacturing seventy per cent. of three noncompeting groups of patented machines collectively used for making a single product than to three

[1] In this case the Supreme Court did not find that the companies combined were noncompeting; it merely accepted the construction put on the indictment by the lower court. But in 247 U. S. 41, 47, the Court (four judges) did assert that the companies that united to form the United Shoe Machinery Company were not competitive. However, the dissenting opinion (three judges) declared that some of the companies were competitive, and introduced testimony of the leading officials of the company that substantiated this contention (247 U. S. 82–83). The matter is highly important since the decision of the Supreme Court turned on this point. By the majority opinion the United Shoe Machinery Company was declared to be in essence a union of several patent monopolies, which was not forbidden by the Sherman Act. For a discussion of the decisions of the Supreme Court, see pp. 431, 432.

corporations making the same proportion of one group each. The disintegration aimed at by the statute does not extend to reducing all manufacture to isolated units of the lowest degree. It is as lawful for one corporation to make every part of a steam engine and to put the machine together as it would be for one to make the boilers and another to make the wheels." [1]

The law is thus clear. The United Shoe Machinery Company combined in 1899 a number of noncompeting concerns, and established a monopoly of a very important line of shoe machinery. But the patent law contemplates and permits monopoly, hence the act of combination was not illegal. In other words we are dealing here with a patent trust,—a trust supported by legislation. Without criticizing the principle of our patent legislation it must be clear that the existence and power of the United Shoe Machinery Company does not necessarily lend support to the argument that trusts inevitably evolve because of their superior efficiency. The United Shoe Machinery Company would appear to have evolved because a monopoly was profitable, and sanctioned by law.

As to the economics of the matter, there are, as a matter of course, more or less plausible arguments advanced for a shoe machinery trust protected by patents (as there are for every other trust), as, for example, the following: "Shoe manufacturing had become a highly complicated industry. In making Goodyear welt-shoes, one hundred and eighty-five distinct operations were necessary, of which one hundred and fifty-seven were machine operations. Few machines could perform more than one or two of these operations. In every shoe factory, therefore, a great many different machines had to be assembled, adjusted to work in absolute harmony, and kept in perfect operation. If any machine broke down or got out of adjustment, the industrial chain was broken, and all the machinery in the factory had to stand idle until the broken link was restored. The shoe manufacturer, consequently, was always at the mercy of his weakest machine. His product was always

[1] 227 U. S. 217–218. The validity of the leases with their tying clauses (see pp. 171 ff.) was not before the court in this case.

limited by the delay and inadequacy of the service furnished by the weakest manufacturer from whom he obtained machinery. Every other machinery manufacturer, whose machines were prevented from earning royalties during this enforced idleness, was also a sufferer. He, no less than his customer, was always at the mercy of the weakest machines in his customer's factory. His royalties from his machines were always limited by the delay and inadequacy of the service which his competitor furnished to their common customer.

"Such instability could not endure. Breakdowns multiplied; repair bills became intolerable; continuous operation was never certain; production costs could never be predicted; promises of definite deliveries could not be fulfilled; machines bought outright soon became worthless; large customers demanded and frequently obtained rebates over their smaller competitors; enforced idleness caused by inefficient machinery service resulted in frequent turmoils of factory operatives; an up-to-date shoe factory involved such large, unforeseeable outlays as to become almost a financial impossibility." [1]

However accounted for, it gradually came about that the making of machinery for the bottoming operations in shoe manufacture centered in three noncompeting groups. The movement might have stopped there. The concentration of the bottoming machinery in the hands of three concerns would have obviated many of the difficulties referred to above, as it would naturally have been to the decided interest of each of these concerns to permit continuous use of their machines. But the movement went on, and in 1899, as we have seen, the three groups united to form the United Shoe Machinery Company. The formation of this company was legal, and, according to the Supreme Court, "on the face of it simply an effort after greater efficiency." Probably efficiency would have been equally promoted, and the public interest better protected, by the existence side by side of several concerns, each making a full line of bottoming machinery, though one must not speak too dogmatically on the basis of

[1] Roe, Journal of Political Economy, 21, pp. 941–942. For the opposing view see Brief for the United States (no. 207), pp. 226–229.

present knowledge. Furthermore, it would be quite possible, if public opinion is opposed to patent trusts, to have the federal government acquire the patent rights on its own account, and throw open the invention to general use, due compensation being made to the inventor to reward him for his labor and financial outlays. While invention will be stimulated and industrial progress promoted by proper encouragement in a financial way to inventors, it is by no means certain that that encouragement could not be given without permitting at the same time the establishment of patent monopolies.[1] If then it appeared that it were more efficient for all the machinery in a given shoe factory to be owned by one company, it would still be possible for individual manufacturers to lease all their machinery from one company, with the alternative, however, of turning to other manufacturers upon the expiration of the leases, in the event that the service was not satisfactory. By this arrangement the government would hold the patents, and active competition in the business of manufacturing shoe machinery and supplying shoe machinery service would be possible, as it is not now, because of the fact that many of the essential patents are owned by one company.

In the second place, the strength of the United Shoe Machinery Company was the result of the so-called tying clauses in its leases. The United Company did not sell its principal machines; it merely leased them to shoe manufacturers at a royalty of so much per pair of shoes. The provisions of the leases are very important, and deserve detailed consideration. For this purpose we shall take the leases for lasting machines,—one of the essential machines.

The principal provisions of the lasting machine leases are (in substance and condensed form):[2]

Sec. 1. The leased machinery shall at all times remain the

[1] It should be realized that a monopoly in shoe machinery of certain types is likely to discourage invention, since there will be no competition for the product of the inventor, and his reward will therefore be limited.

[2] A copy of a lasting machine lease is in the Report of the Senate Committee on the Control of Corporations, pp. 2170–2174.

exclusive property of the lessor (the United Company). The lessor and its agents and employees shall at all times be given access to the leased machinery for the purpose of inspecting it, watching its operation, repairing it, or determining the extent of its use.

Sec. 2. The lessee (the shoe manufacturer) shall at his own expense keep the leased machinery in good working order. He shall obtain from the lessor exclusively, and shall pay therefor at the regular prices from time to time *established by the lessor*,[1] all the duplicate parts and extras needed in operating or repairing the leased machinery.

Sec. 5. The leased machinery shall be used for no other purpose than for lasting shoes or other footwear made by or for the lessee. The leased machinery shall not, nor shall any part thereof, be used in the manufacture of any welted shoes or other footwear, or portions thereof, which have been or shall be welted in whole or in part, or the soles of which have been stitched, by the aid of any welt-sewing or sole-stitching machinery not held by the lessee under lease from the lessor; or in the manufacture of any turned shoes or other footwear or portions thereof, the soles of which have been or shall be in whole or in part attached to their uppers by the aid of any turn-sewing machinery not held by the lessee under lease from the lessor; or in the manufacture of any shoes or other footwear which have or shall be in whole or in part pulled over, slugged, heel seat nailed, or otherwise partly made by the aid of any pulling-over or "Metallic" machinery not held by the lessee under lease from the lessor. Subject to the foregoing limitations, the lessee shall use the leased machinery to its full capacity upon all shoes or other footwear, or portions thereof, made by or for the lessee in the manufacture of which such machinery is capable of being used.

Sec. 6. The lessee shall pay to the lessor as royalty the sum of 1 1/4 cents for each pair of shoes or portion thereof lasted by the aid of the leased machinery.

Sec. 8. If at any time the lessee shall fail or cease to use *exclusively* [2] lasting machinery held by him under lease from the

[1] Italics supplied by the author. [2] Ibid.

lessor for lasting all shoes made by him or for him which are lasted by the aid of machinery, the lessor may at its option terminate forthwith, by notice in writing, any or all leases of lasting machines then existing between the lessor and the lessee; and the possession of the lasting machine shall thereupon be revested in the lessor free from any claims whatever.

Sec. 9. This lease shall continue, unless sooner terminated by the lessor because of breach thereof on the part of the lessee, for seventeen years. But if any breach shall be made in the observance of any one or more of the conditions contained herein or contained in any other lease subsisting between the lessor and the lessee, the lessor shall have the right, by notice in writing to the lessee, to terminate forthwith *any or all*[1] leases to use machinery then in force between the lessor and the lessee. Upon the expiration of this lease or its termination by notice, the lessee shall forthwith deliver the leased machinery to the lessor at Beverly, Massachusetts, in good order; and shall thereupon pay to the lessor the sum of $150 in respect to each lasting machine hereby leased, as partial reimbursement for deterioration of the leased machinery.

Sec. 10. In case at any time the lessee shall have in his possession more lasting machines than, in the opinion of the lessor, are needed to perform the work which the lessee has for such machines, the lessor may, upon thirty days' notice in writing, terminate the lease to use any one or more of the lasting machines hereby leased. In case any lease is thus terminated, the lessee shall pay to the lessor such sum as may be necessary to put such machine or machines in suitable condition to lease to another lessee.

Sec. 13. The lessee admits the validity for the full term expressed in the grant thereof of each of the Letters Patent of the United States owned by the lessor.

The provisions of this lease bear witness to the power of the United Shoe Machinery Company. Shoe manufacturers would hardly have submitted to such conditions had it not been largely a matter of necessity. It should be borne in mind, however, that it is not the leasing system itself that is the subject of com-

[1] Italics supplied by the author.

plaint; rather it is the tying clauses contained in the leases. The leasing system, in fact, possesses distinct advantages, particularly to the manufacturer of shoes operating on a comparatively small scale. Were it necessary for a shoe manufacturer to buy his shoe machinery, it would require considerable capital to engage in the business. As it is, the machines, with all that is involved in the way of invention costs, depreciation, care of machines, cost of administration, are supplied to the shoe manufacturer at a comparatively small royalty per pair of shoes. The evidence is that the United Company has given the same terms and the same service to every shoe manufacturer, no matter whether he was doing business on a large scale or on a small scale; that a larger capital has never availed to secure any favoritism with respect to machines and machine service.[1] As the result of this policy competition has continued quite active in the shoe industry.

Since it is not the practice of leasing machinery that is complained of, but rather the tying clauses in the leases, it will be advisable to consider more fully the nature of these tying clauses and their significance.

According to section five of the lasting machine lease described above a shoe manufacturer leasing a lasting machine from the United Shoe Machinery Company obligated himself not to use that machine in the manufacture of shoes which have been or shall be welted in whole or in part with the aid of any welt-sewing machinery not held by the manufacturer under lease from the United Company; nor in the manufacture of shoes, the soles of which have been in whole or in part stitched with the aid of sole-stitching machinery not leased from the United Company; nor in the manufacture of turned shoes, the soles of which have been or shall be in whole or in part attached to their uppers with the aid of any turn-sewing machinery not leased from the United Company; nor in the manufacture of shoes which have been or shall be in whole or in part pulled over, slugged, or heel seat nailed with the aid of any machinery not leased from the United

[1] Report of the Senate Committee on Control of Corporations, pp. 1160, 1964, 2159.

Company. The crux of the whole matter is that the shoe manufacturer had to have a lasting machine; for all practical purposes he could get one only from the United Shoe Machinery Company; [1] and if he leased one from the company—it would not sell him one under any circumstances—he had to agree to use certain other machines of the company, notably the welter, stitcher, and metallic-fastening machines. That is, to the essential machines, like the laster, other machines were tied. These other machines might not be as good as those of competing shoe machinery manufacturers—it is not intended, of course, to say that they were not—but if the shoe manufacturer wished to use a laster he had but little choice. This, in effect, restrained him in the use of competing shoe machinery. The government in its petition asking that the court declare these tying clauses illegal under the Clayton Act [2] charged that competitors of the United Company were prepared to supply certain kinds of shoe machinery at lower prices or royalties than were asked by the United Company, but that the shoe manufacturers were deterred from buying or leasing them by the tying clauses, and by the fear of the serious financial consequences that would attend their violation.[3] Competition in the manufacture of shoe machinery was thus rendered largely impotent by the tying clauses.

Counsel for the United Shoe Machinery Company has stated the theory of the tying clauses: "The fundamental machines are

[1] President Winslow testified that "after the formation of the United Company it was manufacturing every single lasting machine that was being put out in the United States except the Seaver machine; and in 1900 we acquired the Seaver Company" (247 U. S. 81). At the time of the government suit only one other concern—the R. H. Long Machinery Company—professed to put out lasting machines. Yet this company had put out only four, and it was by no means in a position to supply all the requisite types of lasting machines. That being the case it could not become a competitor of any consequence, since all of the United Company lasting machine leases contained an exclusive use clause, which required the shoe manufacturer to obtain all of his lasting machinery from the United Company. Brief for the United States (no. 207), pp. 177–178.

[2] See p. 476.

[3] Original Petition in United States *v.* United Shoe Machinery Company, p. 12.

the stitcher and welter, which attach the upper to the inner sole and the outer sole to the welt. To those fundamental machines other machines are tied. A man can have a stitcher and a welter and not be required to take a single other machine, and he can acquire by purchase a great number of other machines without being required to take a stitcher or a welter. But if he takes a stitcher and a welter and also wants to take a lasting machine he is required to use that lasting machine only on shoes which are stitched and welted on the company's stitcher and welter." [1] According to counsel a shoe manufacturer could have a stitcher and welter, and need take no other machine.[2] But he had to have a lasting machine, and if he took one—as he must if he is to manufacture shoes—he was required in effect to use not only the company's stitcher and welter, but a number of other machines, none of which might be used except in connection with the company's lasting machines. The privilege, therefore, of using the company's stitcher and welter and no other machine was thus a hollow one.

It is important to note that through these tying clauses the period of patent protection has in effect been extended beyond the time set by law. A machine on which the patent has expired can be tied to an essential machine on which the patent has not expired. Mr. Charles H. Jones testified that his company was paying at least $25,000 a year royalty on machines, the important patents on which had already expired.[3] It would appear that so long as the tying clauses are in force, the time may never come when shoe manufacturers will be free to secure their bottoming machinery where they choose. In other words, potential competition may hardly be said to exist in this industry.

The attitude of the shoe manufacturers generally appears to be one of opposition to the tying clauses. The Shoe Manufacturers' Alliance, comprising manufacturers producing about 40 per cent of all the shoes produced in this country, adopted resolutions in

[1] Report of the Senate Committee on Control of Corporations, p. 2166.

[2] The lessee of a welter may not use a competing stitcher and vice versa. Brief for the United States (no. 207), p. 182.

[3] Report of the Senate Committee on Control of Corporations, p. 2271.

1911 urging the removal of the tying clauses and the restoration of competitive conditions in the shoe machinery industry.[1] The Shoe Manufacturers' Association of Brockton, one of the shoe centers of New England, passed a resolution in 1911 that the association place itself on record as being in favor of a continuance of the lease system of the United Company, provided such portions of the leases as operated to exclude the use of competitive machines were abolished, and provided the penalty or charges for returning used machinery were modified or wiped out.[2] This association represented at least 10 per cent of the shoe manufacturers of the country. Mr. Charles H. Jones, a prominent shoe manufacturer in Boston, testified as follows before a Senate investigating committee: "I believe I am well within the fact when I say there are not a dozen men in the United States engaged in the manufacture of shoes who do not believe this tying clause should be stricken out. They like some of the features of the leasing system very much, but all agree that these things are repugnant to common sense and good business practice." [3]

In 1907 the state of Massachusetts passed a bill to make the tying clauses illegal. The act provided in substance that no person, firm, or corporation should make it a condition of the sale or lease of any tool, appliance, or machinery, that the purchaser or lessee thereof should not buy, lease, or use machinery, tools, appliances, material or merchandise, of any person, firm, or corporation other than such vendor or lessor; but this provision should not impair the right, if any, of the vendor or lessor of any tool, appliance, or machinery protected by a lawful patent right vested in such vendor or lessor to require by virtue of such patent right the vendee or lessee to purchase or lease from such vendor or lessor such component parts of said tool, appliance, or machinery, as the vendee or lessee might thereafter require during the continuance of such patent right: Provided, that nothing in the act should be construed to prohibit the appointment of sales agents to sell or lease machinery, etc.[4]

[1] Report of the Senate Committee on Control of Corporations, p. 2266.
[2] Ibid., p. 2121. [3] Ibid., p. 2263. [4] Acts of 1907, ch. 469.

Thereupon the United Company attached to all its leases a rider providing that "any and all agreements, stipulations, provisions, and conditions hereinbefore printed in this instrument which are in violation of the provisions of Chapter 469 of the Acts of the General Court of Massachusetts for the year 1907, if there are any such, are hereby stricken out before execution and are not agreed to nor made a part of this contract." [1]

The Massachusetts legislation thus seems to have had but little effect. The right reserved to the United Company to cancel all leases apparently deterred the shoe manufacturers from putting to the test their undoubted legal rights; for a manufacturer who attempted to use in part only the essential machinery of the United Company ran the risk of ruin.

In 1914, as part of the anti-trust legislation of that year, the federal government enacted a similar prohibition. This topic will be discussed in chapter XV.

The United Shoe Machinery Company has laid a great deal of emphasis upon the excellence of its machines and of its service; and there can be no doubt that such excellence has been a great asset. Mr. McElwain, late president of the largest shoe concern in the country, said in a letter (1912): "We believe that the United Shoe Machinery Co. is in many respects rendering efficient service to shoe manufacturers. . . . We have sufficient confidence in the strength of this company to believe that it will stand in the forefront of shoe machinery makers, even with the removal of the restrictions, which have been mentioned [the tying clauses]." [2] Its high efficiency was commented upon freely also by the Circuit Court before which the dissolution suit was tried.[3]

Whether the existence of a shoe machinery trust promotes invention, however, is a disputed question. The United Company maintains a large corps of inventors, and, according to counsel for the company, has made distinct progress in invention. "The United Shoe Machinery Company has spent all the way from $250,000 to $750,000 in experiment and development of new

[1] Journal of Political Economy, 21, pp. 945–946.

[2] Report of the Senate Committee on Control of Corporations, p. 2268.

[3] 222 Fed. Rep. 372.

machines every year since it was formed. It has made workable over 100 different new machines, some of which perform operations formerly performed by hand and all of which are far better than those formerly in use. Taken in connection with reduction in royalties, shoe manufacturers by their use effect a saving of nearly 9 cents in the cost of making a pair of Goodyear welt shoes, or nearly double the royalty now paid. A greater number of practical patents in shoe machinery have been made effective in the past 12 years than in any other period of equal length since shoe-making began." [1]

That the technical progress of the industry has been promoted by the United Company is denied by prominent shoe manufacturers. A group of them instrumental in organizing the Shoe Manufacturers' Alliance made the following statement: "At present [1912] practically all of the essential machinery used in bottoming shoes in this country is owned by a single corporation, which is dominated practically by one man. This is a condition permitting the exercise of complete and arbitrary control of our businesses. It is contrary to the very spirit of liberty, and as such humiliating to us as shoe manufacturers. It also necessarily tends to retard and to restrict improvements in shoe machinery.

"That it does so restrict development will be clear to those who compare the progress of shoe machinery during the last 12 years with the advances made from year to year prior to that date. Shoe manufacturing in America is to-day efficient, and much of that efficiency is due to the extraordinary advances in shoe machinery made prior to the organization of the Shoe Machinery Trust. Nearly every one of the 30 years prior to 1900 witnessed some marked advance in shoe machinery. That was a period of open competition in the production of shoe machinery. Those who controlled the successful inventions reaped rich rewards. The activities of inventors and mechanics were stimulated, and the results were revolutionary in character. Wages increased, but the unit labor cost of producing shoes was being continually and substantially lowered.

"Since 1900 the development in essential shoe machinery has

[1] Roe, Journal of Political Economy, 22, p. 55.

not been marked by any important invention materially reducing the cost or improving the quality of work. Such new inventions as have been made are confined to details of minor consequence as compared with the advances made prior to the formation of the Shoe Machinery Trust. This check upon the development of essential shoe machinery is believed to be a necessary result of the formation of the combination. It has removed the stimulus of competition." [1]

Mr. Charles H. Jones testified that it was the belief of men in the shoe business and in the shoe machinery business that the inventors of the United Company were allowed to work only along very narrow lines, and that they were not encouraged to develop original ideas.[2] In fact, so he said, "it is directly against the interests of this company, in its machinery investments, to find revolutionary machines. They have got 90,000 machines, they claim, in the factories of the United States. These machines are producing them an enormous revenue. What possible inducement would it be for them to throw out one, two, or three of those machines and put in something very much better? They could not get any more royalty. They would have a very large machinery cost, but there would be no additional return." [3]

That the United Shoe Machinery Company possessed no monopoly of inventive genius is proven by the Plant episode.[4] Mr. Thomas G. Plant, a shoe manufacturer at Roxbury, Massachusetts, succeeded in inventing a set of bottoming machinery which, to say the least, had great experimental promise. The business of the shoe machinery trust, protected as it was by patents, bade fair to be interfered with, when the whole outfit, including Mr. Plant's shoe factory, was purchased (1910) by the United Shoe Machinery Company for $6,000,000.[5]

[1] Report of the Senate Committee on Control of Corporations, pp. 2266–2267.

[2] Ibid., p. 2264.

[3] Ibid., p. 2117.

[4] This episode is described in Brief for the United States (no. 207), pp. 105–133.

[5] $3,000,000 in cash and the balance in stock of the United Company having a par value of $1,500,000, but a market value of $3,000,000. 247 U. S. 49.

We will let Mr. Brandeis (now Justice of the Supreme Court) tell the story:

"He [Mr. Plant] was a very successful shoe manufacturer—a remarkably successful man. His concern was earning five or six hundred thousand dollars a year. His business had been built up through his own efforts and with his brother's aid. With a few about him he displayed admirable business ability, governing a business extending throughout the country. He undertook a task which was large, namely, of creating a competing shoe-machinery system, and it involved the expenditure of several million dollars—between three and four million dollars. Now, with Mr. Plant's shoe business and with these machines which he had developed into a successful system—declared by some of the best manufacturers of the country to be superior to the United's—he was in a position where he was entitled practically to any reasonable credit he might ask. The amount that he required to carry him along was about $2,000,000. He had property that was worth four or five million dollars. His shoe business was one of the leading shoe businesses in the country, and yet after he had completed his machinery system; after he had demonstrated the success of it and gotten the certificate of approval from some of the best manufacturers of the country, east and west, his credit was cut off absolutely. Men who were disposed to give credit after a few days withdrew."

"That was not accident. It was not the result of internal deliberation upon the question. It was undoubtedly the result of that influence exercised directly and indirectly by the powerful organization to which he was opposed. As a matter of fact this shoe machinery corporation is a financial power as much as it is an industrial power. The managers of the shoe machinery corporation are practically the controlling influence in the First National Bank of Boston. They are a very large influence in our leading trust company, and have important influence in the Hanover National Bank and other banks of New York. It has been the steady policy of the United Shoe Machinery Corporation to keep at all times a huge cash balance which was deposited in those various banks, evidently not so much for current use in the

business as for the financial control which they exercised through being large depositors in important banks . . . . I have very good evidence—absolutely reliable in my judgment—that one of the men who refused Mr. Plant credit, thought that his credit was perfectly good and was willing to give him the credit, but was not willing to oppose the important financial interests that intimated to him that they did not want him to have credit. . . . . You know how he happened to sell out his business to the Shoe Machinery Trust. Mr. Plant was driven to the position where the next day he had to meet perhaps half a million dollars of obligations and he simply could not get any money. He had been driven to the last ditch. He had been trying to raise some money through an arrangement with western manufacturers. They were in Boston for that purpose. They were not quite ready to agree to advance the large sum of money needed. It was necessary to have about a million dollars to meet the situation. He left these western manufacturers at about 8 o'clock. Failure to meet his obligations stared Mr. Plant in the face. He then went to the office of the counsel of the Shoe Machinery Trust to see the members of that corporation, and between 8 that evening and 5 o'clock the next morning the transaction was completed by which this wonderful competitive machinery system was turned over to the shoe machinery corporation. The officers and counsel were in conference all night to complete the transaction which involved something like $5,000,000, enough to enable Mr. Plant to pay his debts and to remain a rich man." [1]

Thus, said Mr. Brandeis, even in the ably managed United Shoe Machinery Company the inefficiency which is bred of monopoly manifested itself.[2]

The charge of banking pressure has been denied by representatives of the company. The president in a letter to the Senate Committee before which Mr. Brandeis told his story wrote that "the United Shoe Machinery Co., or anyone connected with it, never did anything to injure Mr. Plant's credit at the bank or to in any way affect banks in regard to Mr. Plant." [3] Representa-

[1] Report of the Senate Committee on Control of Corporations, pp. 1188–1190. [2] Ibid., p. 1161. [3] Ibid., p. 1960.

tives of the company further charged that Mr. Plant's inventions in their then existing form could not have been utilized to the best advantage by the trade, but combined with the inventions owned by the United Company and incorporated in its machines they would advance the art of shoe-making materially.[1] In fact—so they charged—Mr. Plant had no desire to supply the shoe manufacturers with machines; he had built up his line of machines to sell to the United Company.[2] Whatever may be the merits of this controversy, it is admitted by counsel for the company that the improvements made by Mr. Plant were worth every cent that they cost the company; [3] and it would appear to be proven, therefore, that the United Company, with all its corps of inventors, did not entirely take the place of independent endeavor in promoting the technical progress of the industry.

The profits of the United Shoe Machinery Company come largely, of course, from the royalties on the use of the leased machines. The number of machines on lease in the United States on March 1, 1911, was 90,276.[4] According to the president of the company, the amounts paid per pair of shoes for the use of all the principal royalty machines furnished by the company for the manufacture of the different classes of shoes, when accounts were paid within thirty days, were substantially as follows: [5]

Goodyear welts, men's work	$0.05694
Goodyear welts, women's work	.04694
Goodyear turn shoes, women's and misses'	.01972
Goodyear turn shoes, children's	.00500
McKay shoes, men's and women's	.01746
McKay sewed shoes, children's	.01391

[1] Report of the Senate Committee on Control of Corporations, p. 1959. See on this point 247 U. S 50–51, 87–89.

[2] Report of the Senate Committee on Control of Corporations, p. 2162. Judge Dodge of the Circuit Court declared this charge to be true. 222 Fed. Rep. 376.

[3] Report of the Senate Committee on Control of Corporations, p. 2162.

[4] Annual Report of the United Shoe Machinery Company, 1911, p. 5.

[5] Ibid., p. 7.

From these royalties there should be deducted six-tenths of a cent per pair for men's Goodyear welts, forty-five one-hundredths of a cent per pair for women's Goodyear welts, and seventy-five one-hundredths of a cent per pair for women's and children's Goodyear turns; the foregoing sums to be invested in stock of the company, and given to lessees.[1] This profit-sharing plan, presumably designed to secure the adhesion of the shoe manufacturers, was subsequently abandoned (1912) because—so it was alleged—of the government dissolution suit filed in December, 1911.

The foregoing royalties, according to the president, covered substantially everything that the company received for the use of its principal machines from those manufacturers who used its machines in making Goodyear welt, Goodyear turn or McKay sewed shoes.[2] In return for the royalties and rentals which it received, the company assumed the cost of invention, development, manufacture, and depreciation of machines; the care of the machines through its force of over 500 experts, who devoted their entire time to the service; the purchase of patents; and the cost of administration. According to the president, the only important item of cost in the manufacture of shoes which did not increase during the first twelve years after the company was formed was the item of machinery.

The profits of the company have been very liberal. Up to 1905, 6 per cent dividends were regularly paid on the preferred stock and 8 per cent on the common stock. In that year a reorganization was effected. For reasons not clear, a new company—the United Shoe Machinery Corporation—was organized in May to serve as a holding company. The Corporation offered to exchange its preferred stock at par plus 1 1/2 per cent cash for the preferred stock of the United Shoe Machinery *Company*, and 150 per cent of its common stock plus 3 per cent cash for the common stock of the *Company*. This offer was generally

[1] Annual Report of the United Shoe Machinery Company, 1911, p. 7.

[2] A number of auxiliary machines could be used by the shoe manufacturer without payment of royalty, but upon payment of a nominal annual rental to cover the depreciation of the machines.

accepted, and the Corporation by 1915 held 98 1/2 per cent of all the stock of the *Company*.[1] Upon the preferred stock of the Corporation 6 per cent has regularly been paid, and upon the common stock, including the 50 per cent addition, 8 per cent as before. In addition, the common stockholders have received numerous stock and extra cash dividends. In 1907 they received a 25 per cent stock dividend; in 1909 a 10 per cent stock dividend, and 2 per cent extra in cash; and in 1910 a 10 per cent stock dividend, and 4 per cent extra in cash. The total in 1910 was thus 12 per cent in cash plus 10 per cent in stock. On the original common stock, which may have been heavily watered, this amounted to quite a high figure. To be exact, it amounted to $18.15 cash on every $100 of common stock issued by the United Shoe Machinery in 1899, and counting the extra dividend in 1910 to $22.15 in cash. These are dividends only; the profits were much greater, as is evident from the large surplus built up. For example, during the three years ending March 1, 1912, the net earnings aggregated $17,268,000; the dividends $9,344,000; and the surplus $7,924,000.

[1] Moody's Manual, Industrial and Public Utility Section, 1916, p. 3690.

CHAPTER IX

THE UNITED STATES STEEL CORPORATION [1]

With the early history of the iron and steel industry we are not concerned. Even as late as 1890 there were practically no combinations of the modern type in the steel industry. To be sure, the Illinois Steel Company, for example, had been organized in 1889 as a consolidation of three erstwhile competitive concerns, yet such combinations were unusual. During the early nineties, however, the situation changed. The individual plants not only continued to expand in size, as during the eighties, but they became united in combinations. In 1891 the Lackawanna Iron and Steel Company was incorporated, a consolidation of the Lackawanna Iron and Coal Company and the Scranton Steel Company. In 1892 the Colorado Fuel and Iron Company was organized to unite the Colorado Fuel Com-

[1] On the United States Steel Corporation see: Report of the Commissioner of Corporations on the Steel Industry, part I, Organization, Investment, Profits, and Position of United States Steel Corporation (July 1, 1911), part II, Cost of Production, Preliminary Report (January 22, 1912), and part III, Cost of Production, Full Report (May 6, 1913); Brief for the United States, in two parts, in United States *v.* United States Steel Corporation (no. 6214); Brief for the United States, in two volumes, in United States *v.* United States Steel Corporation (no. 481); Brief for the United States Steel Corporation (no. 481); 223 Fed. Rep. 55–179; 251 U. S. 417–466; House Report no. 1127, 62nd Cong., 2nd sess. (Stanley Committee Report); Report of the Senate Committee on Interstate Commerce on the Control of Corporations, 1913; Industrial Commission, vol. I, pp.849–1039, and vol. XIII, pp. 448–516; Berglund, The United States Steel Corporation; Wilgus, A Study of the United States Steel Corporation in its Industrial and Legal Aspects; Willoughby, Quarterly Journal of Economics, 16, pp. 94–115; Meade, Trust Finance, ch. 11; McVey, Yale Review, 7, pp. 302–318, and 8, pp. 156–172; Walker, Quarterly Journal of Economics, 20, pp. 353–398; Taussig, Some Aspects of the Tariff Question, chs. 9–10, 12–13; Dunbar, The Tin-Plate Industry.

pany and the Colorado Coal and Iron Company.[1] In the same year the Carnegie Steel Company (Ltd.), a partnership, was formed with a capital stock of $25,000,000. This concern, with all its plants concentrated at Pittsburg, was then the largest in the industry. Yet it could hardly be considered a real combination, since it represented for the most part simply a more binding union of interests long affiliated. Other important concerns in the iron and steel industry in the early nineties were Jones and Laughlin; the Pennsylvania Steel Company, with its subsidiary, the Maryland Steel Company; the Tennessee Coal, Iron and Railroad Company; the Cambria Iron Company; and the Bethlehem Iron Company.

Most of the above enumerated concerns were engaged chiefly in the production of semi-finished steel (billets, blooms and slabs), and of the simpler and heavier forms of rolled steel products, such as rails, plates, and beams. The manufacture of the heavier steel products was concentrated to a considerable extent, even in the early nineties, in the hands of a comparatively few producers. Thus the Carnegie Steel Company, the Illinois Steel Company, the Jones and Laughlin interests, the Lackawanna Iron and Steel Company, the Pennsylvania Steel Company, the Cambria Iron Company, and the Bethlehem Iron Company together turned out nearly half of the steel ingots produced in this country (steel ingots are the raw material from which nearly all steel products are made, but they are generally put through a further process of manufacture before being sold). But these companies were entirely separate with respect to ownership, and in spite of the existence of pools of one kind or another were quite active competitors.[2]

Save these companies producing the heavier steel products, there were comparatively few concerns of any considerable size in the iron and steel industry in the early nineties, and very few

[1] The Colorado Fuel and Iron Company at this time, however, had a greater interest in the coal trade than in the iron and steel business.

[2] Report of the Commissioner of Corporations on the Steel Industry, part I, p. 65. Referred to hereafter as Report of the Commissioner of Corporations.

combinations. The Consolidated Steel and Wire Company, to be sure, was an important combination in the wire and nail business (1892), yet for the most part the manufacture of such products as nails, tin plate, and sheets was carried on by numerous concerns, many of them producing on a small scale. Competition in these lines was quite vigorous, except when restrained on occasion by pooling agreements.

The situation was the same in the iron mining industry. While there were a few large concerns, such as the Minnesota Iron Company and the Lake Superior Consolidated Iron Mines, organized in 1882 and 1893, respectively, yet in general the ownership of the iron ore mines was widely scattered; and though there were iron ore pools, competition was the characteristic feature of the industry.

In another respect the steel industry of the early nineties presented a marked contrast with the industry of to-day. This was in the comparative absence of integration,—the practice of uniting under one control the successive stages in the manufacture of the finished products. There was some integration, to be sure. The Carnegie Steel Company, for example, through the Frick Coke Company held large deposits of coking coal, and by the purchase in 1892 of a half-interest in the Oliver Iron Mining Company had provided itself with a supply of iron ore. But the production of the Oliver concern was quite inadequate to the needs of the Carnegie Company, and, moreover, Mr. Carnegie was understood to be opposed to the ownership of ore mines.[1] The business of mining iron ore, like the production of crude oil, was largely speculative; and Mr. Carnegie, like Mr. Rockefeller, was willing that the risks be borne by those more speculatively inclined. Other companies had integrated their business slightly, yet generally speaking it was true that the manufacturers of finished products bought the semi-finished steel which constituted their raw material; the manufacturers of steel in turn bought their pig iron; and comparatively few iron and steel manufacturers possessed large iron ore deposits or iron ore railroads. The separate stages in the process of production

[1] Report of the Commissioner of Corporations, part I, p. 68.

were not at that time united under one management as at present.

From what has been said it is apparent that the leading characteristic of the iron and steel industry during the early and middle nineties was its competitive character. It is true that agreements were quite common; indeed, there was hardly any branch of the iron and steel industry that was free from them. Yet the pools generally maintained but a precarious existence, and this was especially true of the less formal "gentlemen's agreements."

In the latter part of the nineties, however, the situation underwent a marked change. In 1898 the combination movement struck the iron and steel industry, and by 1900 a large number of combinations had been formed. Some idea as to the extent of this movement is given by the following table, which shows the leading iron and steel combinations created during 1898 to 1900, with their authorized capitalization.[1]

LEADING COMBINATIONS IN THE IRON AND STEEL INDUSTRY, 1898–1900

A. Combinations later united in the United States Steel Corporation

Name and year of organization	*Capitalization*
1898	
American Steel and Wire Co. of Illinois[2]	$ 24,000,000
Federal Steel Co.	230,217,179
American Tin Plate Co.	50,273,000
1899	
American Steel and Wire Co. of New Jersey	90,130,656
American Steel Hoop Co.	33,000,000
National Steel Co.	61,561,000
National Tube Co.	80,000,000
1900	
American Bridge Co.	70,156,000
American Sheet Steel Co.	54,000,000
Carnegie Co. of New Jersey	345,081,813
Shelby Steel Tube Co.	15,000,000
Total	$1,053,419,648

[1] Report of the Commissioner of Corporations, part I, pp. 80–81.

[2] This company was merged in 1899 into the American Steel and Wire Co. of New Jersey.

B. Combinations not subsequently united in the United States Steel Corporation

Name and year of organization	*Capitalization*
1898	
American Car and Foundry Co.	$ 60,000,000
American Iron and Steel Manufacturing Co.	20,000,000
Empire Steel and Iron Co.	10,000,000
National Enameling and Stamping Co.	30,600,000
Pressed Steel Car Co.	25,000,000
Republic Iron and Steel Co.	55,000,000
Sloss-Sheffield Steel and Iron Co.	23,835,000
United States Cast-Iron Pipe and Foundry Co.	30,000,000
Virginia Iron, Coal and Coke Co.	20,000,000
1900	
Crucible Steel Co. of America	50,000,000
Total	$324,435,000

In addition to these combinations there were a number of others in the machinery trade or similar branches of the industry. Among them were the American Bicycle Company, capitalized at $30,000,000; the International Steam Pump Company ($27,500,000); the United Shoe Machinery Company ($25,000,000); the Otis Elevator Company ($11,000,000); and the American Radiator Company ($10,000,000).

The first table shows the companies which subsequently united to form the United States Steel Corporation. A brief description of these companies will facilitate an understanding of the subsequent course of events.

Carnegie Company of New Jersey. The leading concern in the iron and steel industry, without a doubt, was the Carnegie Company of New Jersey. This company was organized in March, 1900, being simply a reorganization of the Carnegie interests and of the H. C. Frick Coke Company (owning extensive coking coal properties in the Connellsville district of Pennsylvania). It had an authorized capitalization of $320,000,000, half stock and half bonds.[1] All of its manufacturing properties

[1] Not counting $25,081,813 of underlying indebtedness represented by bonds.

were concentrated in the vicinity of Pittsburg, thus giving compactness to its organization. The Carnegie Company also derived strength from the fact that its size had been attained largely through internal expansion, rather than through the acquisition of competitors, the purchase of the Duquesne works (1890) being the most important exception. The company was noted for its efficiency, its financial power, and its conservative management. It had built up its property chiefly out of earnings; its securities were not on the stock market; and its owners were actively engaged in the business. Among its more important subsidiary and allied concerns were the Oliver Iron Mining Company, the ore deposits of which, together with those secured by the lease of the properties of the Lake Superior Consolidated Iron Mines, assured the Carnegie Company an ample supply of good ore for a long time; the Pittsburg, Bessemer and Lake Erie Railroad, running from the Great Lakes to Pittsburg, and used mainly for the transportation of iron ore; the Union Railroad Company, operating an important belt line in the Pittsburg district; and various gas, water, and dock companies.

The chief business of the Carnegie Company was the manufacture of semi-finished steel for the trade, and of heavy steel products, such as rails, plates, structural steel, bars, skelp, and bridge material. Its leading position is indicated in the fact that in 1900 it produced some 18 per cent of all the ingots produced in the country, its nearest competitor producing only about 15 per cent.[1] The Carnegie Company did not make such finished products as wire, nails, tubes, tin plate, and sheet steel; it merely supplied the manufacturers of these finished products with the necessary crude steel. But it was, nevertheless, in a position to turn out these finished products itself on comparatively short notice, should its customers decide to produce their own crude steel,—a circumstance that later proved to be one of the unsettling factors leading to the formation of the United States Steel Corporation.

The Federal Steel Company. The largest competitor of

[1] Report of the Commissioner of Corporations, part I, p. 87.

the Carnegie Company was the Federal Steel Company, organized in September, 1898. The Federal Steel Company was a consolidation of the Illinois Steel Company, with several steel plants in or near Chicago, and one at Milwaukee; the Lorain Steel Company, with a plant at Lorain, Ohio; the Johnson Company, with a plant at Johnstown, Pennsylvania; and the Minnesota Iron Company, which not only owned large iron ore deposits, but also an iron ore railroad from the mines to the Lakes (the Duluth and Iron Range Railroad), and a fleet of lake vessels by which the ore was carried from the railroad terminus to the lower lake ports. The Illinois Steel Company controlled the Chicago, Lake Shore and Eastern Railway, connecting its various plants in the vicinity of Chicago; and the Federal Steel Company itself acquired the stock of the Elgin, Joliet and Eastern Railway, a line connecting with nearly every railroad entering Chicago. The Federal Steel Company was thus well integrated; in fact, the chief purpose in its formation seems to have been not so much the suppression of competition as the creation of an organization that would be independently situated, not only with respect to its manufacturing plants, but also with respect to its ore, fuel, and means of transportation.

The Federal Steel Company, like the Carnegie Company, produced chiefly billets, steel rails, plates, structural shapes, wire rods, and semi-finished steel for the trade, many of its largest customers being themselves steel manufacturers. At the time of its organization in 1898 it produced about 15 per cent of the country's output of ingots, somewhat less therefore than the output of the Carnegie Company.[1] The Federal Steel Company was generally rated as a Morgan property.

The National Steel Company. Next in importance after the Carnegie Company and the Federal Steel Company was the National Steel Company, organized in February, 1899. The National Steel Company was a consolidation of a number of steel concerns, located mainly in Ohio, and producing in 1899 about 12 per cent of the total output of steel ingots.[2] It pro-

[1] Report of the Commissioner of Corporations, part I, p. 88.
[2] Ibid., p. 89.

duced chiefly semi-finished steel, i. e., billets, sheet bars, and tin plate bars, rather than the finished products. It had an excellent market for its crude steel through its close affiliation with the American Tin Plate Company, the American Steel Hoop Company, and the American Sheet Steel Company, all promoted by Judge W. H. Moore (the organizer of the National Steel Company), and all obtaining their raw material largely from it. The National Steel Company carried integration almost as far as the Carnegie Company and the Federal Steel Company, but differed from them in being also a combination of formerly competitive concerns.

The American Tin Plate Company—the tin plate trust. This company, organized in December, 1898, illustrates a group of combinations formed, not to integrate more fully the business of production (and thus to achieve a more strategic position), but to restrain or exclude competition. It brought together 39 plants, controlling 279 mills, which represented nearly every concern in the country making tin plate.[1] It effected, therefore, a tin plate trust. Having done so, it attempted to strengthen its position by entering into exclusive contracts with the principal manufacturers of rolls and machinery used in the manufacture of tin plate, and thus to oppose an effective obstacle to the construction of competing mills.[2] While this scheme was not altogether successful (the contracts were cancelled in 1902 at the insistence of the Steel Corporation), the company did succeed in maintaining for several years a monopolistic position in its branch of the steel industry.

The American Steel and Wire Company of New Jersey—the wire trust. This company represented another attempt to restrain competition and to make large promoters' profits. The dissolution of the wire nail pool toward the close of 1896 had been followed by marked reductions in prices, and this led to the

[1] Brief for the United States (no. 481), vol. II, p. 170. The United States Steel Corporation admitted that the American Tin Plate Company acquired control of concerns producing 90 per cent of the country's output of tin plate. Brief for the Steel Corporation (no. 481), p. 77.

[2] Brief for the United States (no. 481), vol. II, p. 192.

organization in March, 1898, of a combination,—the American Steel and Wire Company of Illinois. The next year (January) the combination united with most of the remaining wire concerns to form the American Steel and Wire Company of New Jersey.[1] This company produced mainly wire nails, plain wire, barbed wire, and wire fencing; and according to the brief for the government in its suit against the United States Steel Corporation it secured an almost complete monopoly of barbed wire and woven wire, and controlled about four-fifths of the nails and the wire fencing produced in the United States.[2] The American Steel and Wire Company was well integrated, possessing, either at its organization or shortly thereafter, large ore deposits, a big reserve of coking coal, a large fleet of Lake vessels, and facilities for producing a limited amount of pig iron and crude steel.

The National Tube Company—the tube trust. The National Tube Company was incorporated in June, 1899, to monopolize the tubing industry, and incidentally to enable its promoters to make a profit through its organization (one-quarter of its $80,000,000 stock issue was given to the promoters). Its principal product was iron and steel wrought tubing, and the company stated in 1900 that its yearly capacity was 1,000,000 tons, or 90 per cent of the total capacity of the country.[3] While this may have been an exaggeration of the extent of its control, nevertheless the company did produce nearly three-fourths of the country's output of wrought tubing.[4] The National Tube Company, though rated as a Morgan concern, was largely dependent, because of the location of its plants, on the Carnegie Company for the semi-finished steel that constituted its raw material. Subsequently it proposed to produce itself most of its raw material, with consequences soon to be described.

The American Steel Hoop Company. This company was

[1] Report of the Commissioner of Corporations, part I, p. 92.

[2] Brief for the United States (no. 6214), part I, p. 50.

[3] Ibid., (no. 481), vol. II, p. 222.

[4] See Report of the Commissioner of Corporations, part I, p. 92; Brief for the United States (no. 6214), part I, p. 53; and 223 Fed. Rep. 167.

formed in April, 1899. It united nine concerns producing mainly iron and steel bars, hoops and bands, cotton ties, and iron skelp. It was primarily a combination of erstwhile competitive concerns, and, according to the Commissioner of Corporations, a desire to limit competition and afford a large profit to the promoters was undoubtedly the ruling motive in its organization.[1] The promoters received for their services $5,000,000 of the $33,000,000 stock issued by the company, or over 15 per cent of its total capitalization.[2]

The American Sheet Steel Company—the sheet steel trust. This company was organized in March, 1900, to consolidate the properties of the principal manufacturers of sheet steel. Like the American Tin Plate Company it was formed to unite competing concerns; and it secured control upon its organization of about 70 per cent of the country's capacity of sheet steel, the only important product made by it.[3]

The American Bridge Company. This company, like most of those already described, was organized (April, 1900), not to secure the advantages of integration, but the profits arising from a curbing of competition.[4] Its main business was the erection of bridges and of steel construction for buildings, and it was entirely dependent on the large steel manufacturers for its raw material. The American Bridge Company, like the Federal Steel Company and the National Tube Company, had close affiliations with the firm of J. P. Morgan and Company.

The Shelby Steel Tube Company—the seamless tube trust. This company, incorporated in February, 1900, combined practically all the concerns in the country manufacturing seamless tubing.[5] It claimed 90 per cent of the country's output, and there is no doubt that it did have a substantial monopoly of its special product until its field was invaded by the National Tube Company. The motive in its organization was the establish-

[1] Report of the Commissioner of Corporations, part I, p. 91.
[2] Cf. p. 287.
[3] Report of the Commissioner of Corporations, part I, p. 91.
[4] Ibid., p. 93.
[5] Ibid.

ment of a trust; the element of integration was distinctly lacking.

The Lake Superior Consolidated Iron Mines. The combinations and trusts just described were all organized between 1898 and 1900, and each of them became a part of the United States Steel Corporation. One other concern, organized somewhat earlier, deserves mention. The Lake Superior Consolidated Iron Mines, largely owned by Standard Oil interests, was organized in 1893. It manufactured no iron or steel; it was simply an ore producer and a transportation company. It had vast reserves of iron ore, and it owned an important iron ore railroad,—the Duluth, Missabe and Northern. Affiliated with it was the Bessemer Steamship Company, the largest owner of ore vessels on the Great Lakes. The Lake Superior Consolidated Iron Mines, both because of its property and its financial backers, was a very important concern, and its acquisition by the United States Steel Corporation in 1901 greatly strengthened the latter's position.

What is the explanation of this remarkable movement toward combination in the iron and steel industry? The advantages which these combinations might have expected to gain were three-fold: (1) the restriction of competition; (2) a greater degree of integration; (3) stock market profits for the promoters.

The large profits that the manufacturers hoped to gain were realized. Aided by the favorable industrial situation, these combinations and trusts were able to put prices up to very high figures. The price of Bessemer pig iron, which had averaged $10.32 per gross ton in 1898, went up to $18.88 per ton in 1899, and to $24.72 in March, 1900. The price of steel billets had been $15.18 per gross ton in 1898; it rose to $29.81 per ton in 1899, and to $33.00 in March, 1900. The price of steel rails averaged $17.63 per gross ton in 1898, $28.13 in 1899, and $35.00 in March, 1900. The price of tin plate averaged $64.08 per gross ton in 1898; the next year it went to $95.48. Prior to the formation of the tube trust the price of tubes had been $30.00 per ton. During 1899 (the year of its formation) the price rose to $67 per

gross ton, and early in 1900 reached its maximum at $89.[1] Further details may be had by consulting the table.[2] It is not meant to imply, of course, that all of these price advances were the result of the formation of combinations and trusts; but it is safe to say that they took full advantage of the favorable industrial situation.[3]

The desire to restrict or eliminate competition was, according to the Commissioner of Corporations, undoubtedly the main reason for the formation of these combinations. Taken as a whole, the iron and steel manufacturers had been very prosperous, but the severe industrial depression which began in 1893 and lasted until 1897 had cut into their profits heavily.[4] The manufacturers were anxious to restore the palmy days, and therefore turned to combination and monopoly as likely to prove

[1] 223 Fed. Rep. 168.

[2] AVERAGE PRICES OF CERTAIN IRON AND STEEL PRODUCTS IN 1898, 1899, AND MARCH AND OCTOBER, 1900 *

Commodity	*Per gross ton*			
	1898	*1899*	*March, 1900*	*October, 1900*
Pig iron †	$10.32	$18.88	$24.72	$13.06
Billets †	15.18	29.81	33.00	16.50
Rails ‡	17.63	28.13	35.00	26.00
Plates †	24.23	49.36	45.25	24.19
Structural shapes (beams) †	26.25	40.49	50.40	33.60
Tin plates §	64.08	95.48	108.42	93.86
Wire nails †	29.91	52.04	71.68	49.28
Bars †	21.32	41.36	50.40	24.42
Sheets (black) †	42.28	60.24	67.20	62.72

* Brief for the United States (no. 481), vol. I, pp. 39, 48.

† F. o. b. Pittsburg.

‡ F. o. b. Pennsylvania manufacturing plants.

§ F. o. b. New York.

[3] For a further discussion, see p. 263.

[4] The competition between the steel manufacturers was not "ruinous." See Jones, Quarterly Journal of Economics, 34, pp. 497–502.

more effective than pools, which were not only industrially unstable, but illegal as well.

A second advantage in combination lay in the possibilities of integration. A company which combined under one management the successive stages in the productive process was able to effect certain economies that were not open to a nonintegrated concern. These economies included a saving in fuel costs (those connected with the reheating of the metal), a saving in the labor and time involved in moving the materials, and the utilization of by-products, especially blast furnace gas. These particular economies, of course, could be availed of only by a vertical combination (an integrated concern); a horizontal combination (a combination of plants making substantially the same product) must justify itself, if at all, on other grounds; must point to other economies than those mentioned. On this phase of the matter more will be said later,[1] but we may note at this point the necessity of keeping clearly in mind the distinction between the economies in producing and selling that were attainable by such of these combinations as did not possess monopolistic power (the Carnegie Company, the Federal Steel Company, and the National Steel Company, for example), and the additional economies that might be secured through the organization of a trust (with monopolistic power), as, for example, the American Tin Plate Company, the American Steel and Wire Company, and the National Tube Company. The economies permitted by integration were notable, and no doubt combinations formed to realize them were in the public interest. Yet, as we have seen, a number of these early steel combinations were not vertical combinations, but horizontal combinations. They were not organized for the purpose of securing the advantages of integration, but the profits of monopoly. As the Circuit Court said: "Properties were assembled and combined with less regard to their importance as integral parts of an integral whole than to the advantages expected from the elimination of the competition which theretofore existed between them." [2]

[1] See ch. 19.

[2] 223 Fed. Rep. 167.

Another gain from integration was the possibility it offered of securing the profits which would otherwise go to the manufacturers or producers of the products at the earlier stages. Here was an opportunity to apply Mr. Rockefeller's maxim, "pay a profit to nobody." The gain was especially worth while because of the possibility that a pool or combination controlling the necessary raw material or semi-finished products might charge unreasonable prices. The company producing its own raw materials was assured an ample supply of them at cost to itself. With it companies not so well fortified could not compete advantageously.

The third advantage offered by the combination was the opportunity of making profits from the sale of the securities of the consolidated companies. The profits which were made in this way were of two kinds: first, those made by the manufacturers themselves; and, second, those made by the promoters. That the promoters had a direct financial inducement to form combinations and trusts is shown by the fact that the promoters of seven of these organizations (Federal Steel Company, National Steel Company, American Tin Plate Company, American Steel and Wire Company of New Jersey, National Tube Company, American Steel Hoop Company, American Bridge Company) received in the aggregate over $63,000,000 in stock as their pay.[1] This was not all profit, to be sure, but to say that the compensation was very liberal is expressing it mildly. The profits were likely to be greater, of course, when the promoters were successful in establishing a trust than when they simply effected a combination possessing no monopolistic power. Some of these iron and steel combinations, as has been shown, belonged to one class; some, to another.

The underlying motive in the formation of the steel combinations and trusts of 1898–1900 was, as we have seen, the restriction or smothering of competition. Yet competition, though greatly restrained in several branches of the steel industry, was not destroyed. Indeed it soon appeared that the formation of these combinations was likely to lead to even more vigorous

[1] See p. 287.

competition than ever. This unexpected outcome was the result of an attempt on the part of some of these combinations to integrate themselves so fully that they would be entirely independent of any other steel concern. To ward off the threatened competitive struggle, the United States Steel Corporation was formed. The circumstances leading up to its formation may be considered in some detail.

The combinations already described may be roughly divided into two groups: (1) the primary group, including the Carnegie Company, the Federal Steel Company, and the National Steel Company, concerns manufacturing chiefly semi-finished steel and the heavy steel products; (2) the secondary group, including the American Tin Plate Company, the American Steel and Wire Company, the National Tube Company, the American Steel Hoop Company, the American Sheet Steel Company, the American Bridge Company, and the Shelby Steel Tube Company, concerns manufacturing chiefly the lighter and more highly elaborated steel products. The companies in the secondary group were largely, some almost entirely, dependent on the primary group for the semi-finished steel which constituted their raw material; while the primary group, in turn, disposed of a large part of its output to the secondary group. There was thus a marked interdependence among the two groups, and for a while all went well.

This state of harmony, however, was not to endure. During 1900 the steel trade suffered a reaction, which made necessary the reduction of expenses, if returns large enough to pay dividends on watered stock were to be realized. Some of the concerns in the secondary group soon proposed therefore to integrate themselves still further, and thus to obtain their raw material at cost. The American Steel and Wire Company of New Jersey, for example, made plans to build additional blast furnaces and a large steel plant. The Carnegie Company and the Federal Steel Company, both of which had just enlarged their works, therefore faced the loss of a market for a considerable part of their output. To protect themselves, they decided to produce the more highly elaborated products, thus making use

of nearly their entire semi-finished steel output and freeing themselves from their dependence on other steel manufacturers. In 1900 the Federal Steel Company proposed to undertake the manufacture of tubes and structural material. In the summer of 1900 it was reported that the Carnegie Company would engage on a large scale in the manufacture of wire rods. In January, 1901, the Carnegie Company announced that it proposed to build at Conneaut Harbor, Ohio, the largest pipe and tube plant in the world.[1] The impression was current that the Carnegie Company would eventually make tin plate, sheet steel, and other finished products. The outcome of this policy of retaliation would clearly be two-fold: first, an increase in the country's productive capacity far beyond its normal consuming power; and, second, an abrupt termination of the monopolistic or semi-monopolistic position attained by the concerns in the secondary group.

A severe competitive struggle thus seemed imminent. And in such a struggle it was generally believed that the Carnegie Company would emerge the victor. This concern was credited with owning the best equipped and best managed steel plant in the country, if not in the world. In self-sufficiency of product it was well ahead of its rivals. In fact, there seems to have been little doubt that from the manufacturing standpoint the Carnegie Company would have proved more than a match for its competitors, many of whom, in their endeavor to monopolize the business, had been obliged to acquire at high prices numerous inferior plants. From the banking and financial standpoint the Carnegie Company was equally well fortified. It had ample capital and credit; and its securities were closely held, hence its owners were uninfluenced by stock market considerations. As Mr. Carnegie had remarked, the partners knew nothing about the manufacture of bonds and stocks; they knew only about the manufacture of steel. The Morgan companies—the Federal Steel Company, the National Tube Company, and the American Bridge Company—naturally had excellent financial backing, but

[1] Brief for the United States (no. 481), vol II, pp. 479-481.

the Morgan financiers were tied up in other lines, particularly railroad enterprises, and they did not welcome a steel war. The Lake Superior Consolidated Iron Mines with Rockefeller support could, of course, have weathered any struggle, but this company was not engaged in steel manufacturing, and therefore was not directly concerned. The remaining companies, however, mostly Moore concerns, were very heavily overcapitalized, and had a highly speculative backing. The promoters of these companies had not yet had sufficient time to unload on the public, and so far as they were concerned a trade war had to be prevented at all hazards. Could the conflict be averted, the promoters could await a favorable opportunity for the disposal of the stocks held by them, and they might even realize some additional profits through the sale of the securities of the consolidated company on the rising market that would follow the restoration of harmonious relations.

The result of this situation was the formation of the present steel trust. On February 25, 1901, the United States Steel Corporation was incorporated under the laws of New Jersey (with an authorized capital stock of $3,000), in accordance with a plan to acquire the securities of the Carnegie Company, the Federal Steel Company, the National Steel Company, the American Tin Plate Company, the American Steel and Wire Company, the National Tube Company, the American Steel Hoop Company, and the American Sheet Steel Company.[1] The offer of the Steel Corporation to exchange its securities for those of the companies named was promptly accepted by a great majority of the stockholders (over 98 per cent in each case); and therefore on April 1 the Corporation filed amended articles of incorporation whereunder its authorized capital stock was increased to $1,100,000,000.[2] By this process of exchange (when completed) the Steel Corporation became strictly a holding company trust. Shortly thereafter it acquired the American Bridge Company, the Lake Superior Consolidated Iron Mines,

[1] Chron., 72, p. 441 (March 2, 1901).

[2] Chron., 72, p. 679 (April 6, 1901). For the terms of the exchange see Brief for the United States (no. 481), vol. I, pp. 54–56.

the Bessemer Steamship Company, and the Shelby Steel Tube Company.[1]

The restriction of competition was plainly the main motive for the formation of the Steel Corporation.[2] We should not be surprised, therefore, to learn that not only was the decline in prices then taking place arrested, but that prices were actually advanced. This is shown by the table below, giving the average monthly price of certain iron and steel products in October, 1900 (just prior to the negotiations leading to the organization of the Steel Corporation), and their price in May, 1901, the first month after the organization of the Corporation.

AVERAGE PRICE OF CERTAIN IRON AND STEEL PRODUCTS IN OCTOBER, 1900, AND MAY, 1901 [3]

(Per gross ton)

Commodity	*October, 1900*	*May, 1901*
Pig iron [4]	$13.06	$16.30
Billets [4]	16.50	24.00
Rails [5]	26.00	28.00
Plates [4]	24.19	35.39
Structural shapes (beams) [4]	33.60	35.84
Tin plates [6]	93.85	93.86
Wire nails [4]	49.28	51.52
Bars [4]	24.42	31.58
Sheets (black) [4]	62.72	71.68

Though the restriction of competition was the controlling motive in the organization of the Steel Corporation, at least two other influences were present. One was the desire to secure large

[1] For a list of the subsidiary concerns controlled by the constituent companies of the United States Steel Corporation, see Brief for the United States (no. 481), vol. II, pp. 753–762.

[2] Judge Woolley in a separate opinion in the steel trust case said that his conclusions of fact and of law were that the *organizers* of the Corporation intended to create a monopoly and to restrain trade. 223 Fed. Rep. 178.

[3] Brief for the United States (no. 481), vol. I, pp. 48, 62.

[4] F. o. b. Pittsburg.

[5] F. o. b. Pennsylvania manufacturing plants.

[6] F. o. b. New York.

profits through the sale of the securities of the new company. This matter is discussed in chapter XII; it will suffice here to point out that the underwriting syndicate realized a profit of $62,500,000 through the promotion of the Steel Corporation.

Another reason for the organization of the Steel Corporation was the desirability of integrating the business more fully, and of securing the economies of the trust form of organization. These two considerations, to repeat, must be sharply distinguished. Complete integration can be secured without resort to a trust, i. e., without attaining a monopolistic position at any stage in the process of production, whereas the economies of the trust form of organization can be secured, of course, only by a trust. The significant inquiry always is: can a trust produce more cheaply than a combination, more cheaply even than a highly integrated combination? If it can, anti-trust legislation is likely to prove futile. Now the organization of the Steel Corporation did lead to a somewhat greater degree of integration. The bringing together under one control of the iron ore mines, the iron ore railroads, the Lake vessels, the coking coal properties, and the plants making all kinds of iron and steel products meant that the Corporation was quite independent of others, and that no profits at any stage in the productive process need to be paid to anyone else. So far as the manufacturing processes were concerned, it is doubtful whether anything particular was gained; the advantages of integration were already about as fully realized by the larger and stronger of the constitutent companies,[1] such as the Carnegie Company, or if not already realized, would have been upon the completion of the extensions proposed in 1900 to 1901.

As to the economies of the trust form of organization detailed information, as usual, is difficult, if not impossible, to secure.[2]

[1] Report of the Commissioner of Corporations, part I, p. 108.

[2] The Bureau of Corporations in part III of its Report on the Steel Industry made a study of the cost of producing various steel products, but its investigation threw no light on the costs of the Steel Corporation as compared with the costs of other large and well integrated concerns. In fact, the Bureau, in order to protect the privacy of business, particularly refrained from giving any figures which would reveal the costs at the several independent plants.

It is probable that the steel trust, simply because it was a trust, did effect certain savings. The combining of so many manufacturing properties under one management probably made possible a more economical subdivision of the business whereby particular plants could specialize on certain products, with a consequent reduction in cost. The distribution of the Steel Corporation's plants also gave it an important advantage with respect to transportation costs; it could ship from the nearest mill, and thus save cross freights.[1] Savings were undoubtedly effected through competition between the managers of the different plants; and a more complete utilization was made of certain by-products, such as blast furnace slag (used in the manufacture of cement), which was formerly a waste product.[2] No doubt, also, the large capital possessed by the Steel Corporation assisted it in developing the export trade—claimed by the promoters to be one of the principal reasons for forming the Corporation—but it does not follow that the amount of capital required could have been supplied only by a trust. How important the above enumerated economies were it is not possible to say, but in view of the rapid growth of the independent concerns, as described later, it is not likely that they were controlling. Certainly few, if any, economies were achieved by the trust in the selling end; selling expenses in the iron and steel trade are a comparatively minor factor.[3] In fact, the Commissioner of Corporations believes, the argument of economy in production was probably brought forward to justify the establishment of the trust, and to promote the sale of the company's securities; the

[1] Mr. Schwab at a dinner held on December 12, 1900, discussed the advantages that might be derived from a combination, and referred specifically to specialization, location of plants near the centers of consumption, competition of the several managements, reduction in overhead expense, and the development of the export trade. He expressed the opinion that from a metallurgical or mechanical standpoint the limit of economies had been reached, or nearly so, so highly perfected had the processes of manufacture become. Brief for the United States (no. 481), vol. II, pp. 508–510.

[2] Brief for the United States Steel Corporation (no. 481), pp. 106–107.

[3] Report of the Commissioner of Corporations, part III, pp. 20–21.

main reason for the organization of the Steel Corporation was certainly the hope of averting the threatening competitive struggle.[1]

The capitalization of the Steel Corporation was enormous. Under its amended certificate of incorporation it issued $304,000,000 of bonds, exclusive of $81,000,000 underlying indebtedness, and was authorized to issue $1,100,000,000 of stock, half preferred and half common. All of the bonds and $425,000,000 of each class of the stock were issued, mainly in exchange for the securities of the companies first acquired.[2] Shortly after its organization the Corporation acquired the Lake Superior Consolidated Iron Mines and other concerns, and as a result its issue of each class of stock increased to over $500,000,000, making a total stock issue of over $1,000,000,000. The Steel Corporation, measured by capitalization, and perhaps by any test, was the largest industrial corporation the country had yet produced.

The company upon its organization controlled three-fifths of the steel business of the country.[3] It produced almost 60 per cent of the pig iron used for steel making purposes, about 66 per cent of the crude steel output, and about 50 per cent of the finished steel products in the manufacture of which it was engaged. It had hundreds of millions of tons of iron ore; over 50,000 acres of the best coking coal lands; over 1,000 miles of railroad, including the iron ore railroads; more than one hundred Lake vessels; and large miscellaneous holdings, such as docks, natural gas and limestone properties. Yet despite its enormous size the Steel Corporation did not secure a monopoly of the iron and steel industry, though in certain lines its position was distinctly monopolistic.[4] This is indicated by the following table,

[1] Report of the Commissioner of Corporations, part I, pp. 108–109.

[2] Ibid., p. 106.

[3] Ibid., p. 109.

[4] That its position was not even more monopolistic in certain lines resulted from the fact that some of the constituent trusts had lost heavily in their percentage of the country's trade since their organization some two or three years previous. See on this point Brief for the Steel Corporation (no. 481), p. 77, and 223 Fed. Rep. 134.

showing the Steel Corporation's computation of its proportion of the country's output of the leading products in 1901.[1]

	Per cent
Pig iron, spiegel and ferromanganese	43.2
Steel ingots and castings	65.7
Rails	59.8
Structural shapes	62.2
Plates and sheets	64.6
Black plate produced in tin mills	79.8
Coated tin-mill products	73.1
Black and coated sheets produced in tin mills	67.3
Wire rods	77.7
Wire nails	68.1
Wrought pipe and tubes	57.2
Seamless tubes	82.8

Among the more important rivals of the Steel Corporation in 1901 were Jones and Laughlin, the Lackawanna Iron and Steel Company, the Republic Iron and Steel Company, the Pennsylvania Steel Company, the Cambria Steel Company, and the Bethlehem Steel Company. The Colorado Fuel and Iron Company because of its location was not an effective rival, though the Steel Corporation conducted negotiations looking toward its acquisition; and the Tennessee Coal, Iron and Railroad Company was at this time chiefly engaged in the production of foundry pig iron.

The capitalization of the Steel Corporation as noted above was enormous. But so was the amount of property acquired. Was the Corporation overcapitalized?

The capitalization of the company in 1901 after the acquisition of the Shelby Tube Company (in August) was as follows:[2]

Steel Corporation bonds	$303,450,000
Underlying bonds	59,091,657
Purchase money obligations, etc.	21,872,023
Preferred stock	510,205,743
Common stock	508,227,394
Total	$1,402,846,817

[1] Report of the Commissioner of Corporations, part I, p. 365. See also p. 214.

[2] Ibid., p. 14.

The Bureau of Corporations made a detailed study of the value of the properties of the Steel Corporation in 1901 in order to determine whether the company was overcapitalized, and if so, to what extent. Three different methods were employed. The first method was an historical study, an analysis of the investment of the constituent companies at the time of their organization. The second method was a mathematical computation, a summation of the market value of the securities of the constituent companies, using the average weekly prices from the date of the organization of these combinations up to December 31, 1900. The market prices during the early months of 1901 were not included, since these were naturally influenced by the prospective organization of the Steel Corporation. This second method represented the estimate put by the public on the securities of the constituent companies, and it therefore reflected the probable earning power of these combinations. The third method was a physical valuation, a detailed estimate of the physical properties of the Steel Corporation by departments of its business, the valuation of the ore properties being made in particular detail. The valuation arrived at by the Bureau by the first method was $676,000,000; by the second method, which included intangible items, $793,000,000; and by the third and more accurate method, $682,000,000.[1]

The conclusion of the Bureau, therefore, was that the entire issue of common stock was water, i. e., had no property back of it; and that a large amount, one-fifth to two-fifths, of the preferred stock was water. Even including the intangible assets, the common stock represented nothing but the hope of monopoly gains. By any reasonable standard, therefore, the Steel Corporation was very heavily overcapitalized.

After 1901, however, the Steel Corporation added greatly to its investment. This it did, first, by the construction of additional plants out of surplus earnings or out of the proceeds of issues of securities; and, second, by the acquisition of competing concerns through the sale of its own securities. The most important piece of new construction was the plant at Gary,

[1] Report of the Commissioner of Corporations, part I, p. 15.

Indiana, the largest steel plant in the world. This plant up to December, 1911, by which date practically all the construction then authorized had been completed, had cost over $62,000,000.[1] Another new steel plant was built in Duluth, Minnesota, and a very large cement works was constructed in Buffington (near Chicago) by the Universal Portland Cement Company, a subsidiary of the Steel Corporation. Other important additions also were made by the Steel Corporation (through its subsidiaries).

The investment of the Steel Corporation has likewise been increased through the acquisition of competing companies. In 1902 the Steel Corporation purchased the Union Steel Company, which held large deposits of iron ore and coking coal; and in 1904 it acquired all the stock of the Clairton Steel Company, then in receiver's hands, but in the possession of important ore and coking coal lands.

But far more important was the purchase in November, 1907, of the Tennessee Coal, Iron and Railroad Company. This company, with its main plant located at Ensley, Alabama, was the most important iron and steel concern in the south. It produced 3 per cent of the country's output of iron ore, 2.9 per cent of the output of coke, 2.4 per cent of the pig iron, 1.1 per cent of the ingots and castings, and 4.3 per cent of the rails.[2] Partly because of the fact that all the essential materials were assembled by nature within a radius of a few miles, the Tennessee Company was able to manufacture pig iron cheaper than it could be made in any other section of the United States.[3] The company was controlled by powerful financial interests; and improvements were then under way to double its steel output and rail capacity. The Tennessee Company made open-hearth steel rails—in 1907 it produced 59.1 per cent of the total output of open-hearth rails—and was thus in a position to profit by the increasing demand for that type of rail.[4] But the most important assets of the Tennessee Company were its enormous hold-

[1] Tenth Annual Report of the Steel Corporation, p. 28.
[2] Report of the Commissioner of Corporations, part I, p. 258.
[3] Brief for the United States (no. 6214), part I, p. 11.
[4] Ibid., (no. 481), vol. II, p. 731.

ings of ore and coal; it owned more iron ore and coal adapted for making steel than any company in the United States except the Steel Corporation.[1] There can be no doubt that the desire to secure these deposits had much to do with the purchase of the company. Moreover, the acquisition of the Tennessee Company made it impossible for it to effect a combination with the Republic Iron and Steel Company and the Sloss-Sheffield Steel and Iron Company, as had been planned, and thus to become an even more formidable competitor of the United States Steel Corporation.

The construction of new plants and the acquisition of competing plants greatly increased the investment of the Steel Corporation. This investment in 1901, as shown above, was $676,000,000. Between 1901 and the close of 1910 the investment increased by $504,928,653, of which amount about $435,000,000 was provided for out of surplus earnings.[2] By December 31, 1910, therefore, the total investment of the Steel Corporation amounted to $1,181,000,000. The capitalization of the company on the same date was $1,468,033,260, or about $287,000,000 in excess of the investment. In other words, about $287,000,000 of the Steel Corporation's stock was still "water." It is apparent that after 1901 the Corporation squeezed out a large part of the water in its stock. In 1901 the amount of water had been $726,000,000, using the actual investment as the basis of calculation, and $720,000,000, using the physical valuation as the basis. By 1910 the amount of water had been reduced to $287,000,000 by the first method of calculation, and to $281,000,000 by the second. All of the water had been extracted from the preferred stock, and about half of the water from the common stock.

To have added so greatly to the value of its property, the earnings of the Steel Corporation must have been enormous. That they were so in fact is indicated by the table below, showing for the years 1901 to 1910—the government dissolution suit

[1] Brief for the United States (no. 6214), part I, pp. 10–11.

[2] Report of the Commissioner of Corporations, part I, p. 49. This increase in the investment was over and above a proper allowance for maintenance, repairs, and depreciation.

was brought in 1911—the total investment of the Steel Corporation in tangible property, the net earnings, and the ratio of the net earnings to the investment.[1]

Year ending December 31	*Total investment in tangible property. 000 omitted*	*Net earnings* [2]	
		Amount. 000 omitted	*Per cent*
1901	$ 698,869	$ 77,741 [3]	14.8 [4]
1902	763,574	121,502	15.9
1903	806,615	94,156	11.7
1904	818,238	62,491	7.6
1905	874,840	112,830	12.9
1906	947,397	143,393	15.1
1907	1,078,763	155,416	14.4
1908	1,090,425	84,793	7.8
1909	1,146,875	120,807	10.5
1910	1,186,982	127,216	10.7
Average	941,258	112,856	12.0

The table shows that the net earnings of the Steel Corporation ranged from $62,000,000 in 1904 (its worst year) to $155,000,000 in 1907 (its best year); and averaged $112,000,000 for the ten year period. By the side of such earnings, the profits of the Standard Oil Company, large as they were, seem small indeed.[5] The table shows further that the profits of the Steel Corporation from 1901 to 1910 averaged 12 per cent on its investment. The average rate of profit, however, underestimates the prosperity of

[1] Report of the Commissioner of Corporations, part I, p. 54.

[2] The net earnings are not those given in the annual reports of the Steel Corporation; the Bureau has revised the Corporation's figures somewhat. Thus, the Corporation deducted interest on its bonds in determining its net earnings; the Bureau restored these interest payments to the net earnings, as it was desirous of finding out what the property actually earned rather than the distribution of earnings among the different classes of security holders. Other changes were made by the Bureau in arriving at its figures of net earnings.

[3] Nine months, April to December.

[4] Indicated rate per annum, based on actual earnings for nine months.

[5] Cf. p. 88.

the Steel Corporation. In the first place, the investment included a large amount of idle property, particularly undeveloped iron ore lands; and this naturally tended to reduce the rate of profit on the investment. But more important, the profit of 12 per cent covered the entire investment, whether that investment was represented by 5 per cent bonds, 7 per cent preferred stock, or common stock. The rate of profit on the investment represented by common stock was of course much higher than 12 per cent. But just how much higher, it is not possible to say; the Bureau found it impossible to make a satisfactory computation.

The net earnings of the Corporation, the sum available for dividends on its common stock, and the percentage earned and paid on its common stock during the years 1901 to 1911 (the year in which the government suit was brought) are shown in the table below.

EARNINGS AND DIVIDENDS OF THE STEEL CORPORATION, 1901 TO 1911

	Net earnings.[1] *000,000 omitted*	*Earned on common stock. 000,000 omitted*	*Earned on common stock Per cent*	*Paid on common stock Per cent*
1901.....	$84[2]	$34	9.08	2.00
1902.....	133	54	10.74	4.00
1903.....	109	25	4.92	3.50
1904.....	73	5	0.99	....
1905.....	119	43	8.53	....
1906.....	156	72	14.34	1.50
1907.....	160	79	15.61	2.00
1908.....	91	20	4.05	2.00
1909.....	131	53	10.59	2.75
1910.....	141	62	12.23	5.50
1911.....	104	30	5.92	5.00

In view of the fact that all of the common stock was "water," this record must have been quite gratifying to the stockholders of the Corporation. How much more so must this have been

[1] After deduction of expenses for ordinary repairs and maintenance, interest on bonds, fixed charges of subsidiary companies, and employees' bonus funds. Cf. p. 211 (note).

[2] Nine months only.

true in 1916, when because of the unusual demands for steel arising out of the war there was earned on the common stock $246,000,000, or 48.46 per cent!

Yet in spite of the large sums expended in the construction of new plants, in spite of the acquisition of important competitors, and in spite of its enormous earnings, the Steel Corporation was not able to maintain the prominent position which it held at its organization in 1901. This is indicated by the table on page 214, showing the proportion of the country's business done by the Steel Corporation in the various lines during the years 1901 to 1910 [1] (the last year prior to the dissolution suit).

With respect to iron ore, the Steel Corporation maintained fairly well down to 1910 the position which it attained in 1901. Regularly after its formation it produced about 45 per cent of the total output of iron ore (1904 was an off year). In 1908 and 1909, indeed, it produced even more proportionately than in 1901, yet this was because of the purchase in 1907 of the Tennessee Coal, Iron and Railroad Company, producing about 3 per cent of the total output of iron ore. But since 80 to 90 per cent of the ore used for steel making purposes comes from the Lake Superior region, the Steel Corporation's proportion of the Lake shipments gives a better idea of its importance as an ore producer. And these figures tell a somewhat different story. In 1901 the Steel Corporation controlled over 61 per cent of the ore shipped from the Lake Superior region; in 1910 only 51 per cent. This points to a relative increase in the business done by the independent element.

In the production of coke likewise the Steel Corporation lost ground after its formation. In 1902—the data are not available for 1901—it produced 37.4 per cent of the country's output of coke; in 1910 only 32.7 per cent. These statistics, however, are for the total output of coke, and not simply for the coke used in the production of iron and steel. The Corporation produced a larger percentage of the coke used in the iron and steel industry

[1] Report of the Commissioner of Corporations, part I, p. 364. The figures for the actual production of the Steel Corporation and of the independents from 1901–1910 are shown on pp. 360–363.

PROPORTION OF COUNTRY'S OUTPUT OF IRON ORE, COKE, AND VARIOUS IRON AND STEEL PRODUCTS CONTROLLED BY THE UNITED STATES STEEL CORPORATION, 1901–1910

From annual statistical reports of the American Iron and Steel Association

	'01	'02	'03	'04	'05	'06	'07	'08	'09	'10
Iron ore:										
Total production	43.9	45.1	43.8	37.9	43.4	43.2	43.3	46.3	45.7	44.3
Shipments from Lake region	61.6	60.4	58.8	53.8	56.0	54.2	54.7	56.0	51.4	51.0
Coke	[1]	37.4	34.2	36.6	37.9	36.5	30.3	31.3	34.6	32.7
Pig iron	42.4	44.3	39.9	44.3	43.8	44.2	41.7	43.2	44.8	43.0
Pig iron, spiegeleisen, ferromanganese	42.9	44.7	40.4	44.6	44.2	44.5	41.9	43.5	45.0	43.3
Ingots and castings:										
Bessemer	70.2	73.9	72.0	69.0	67.4	65.7	64.7	66.2	62.7	61.6
Open-hearth	59.0	52.4	51.0	50.4	51.4	49.6	47.9	48.2	51.8	50.8
Total	66.3	65.7	63.5	61.0	60.2	58.1	56.4	56.1	56.0	54.7
Rolled products:										
Bessemer steel rails	59.9	65.4	65.6	57.2	53.6	52.6	51.6	58.6	57.3	60.2
Open-hearth steel rails	[2]	[2]	[2]	[2]	[2]	[2]	[2]	46.3	57.5	57.4
Structural shapes	62.2	57.9	60.3	55.1	54.6	54.6	54.9	47.1	47.1	51.3
Plates and sheets	64.6	59.4	59.9	58.0	57.4	56.3	55.8	51.9	49.8	48.0
Wire rods	77.6	71.5	73.1	71.3	69.9	71.7	71.5	67.9	69.7	67.3
Bars, skelp, etc.	27.3	31.1	29.8	28.6	31.0	33.8	33.9	31.9	39.4	37.6
Total finished rolled products	50.1	50.8	51.2	47.8	47.3	48.1	47.5	47.1	48.9	48.1
Secondary products [3]:										
Wire nails	65.8	64.8	70.6	67.0	66.1	65.5	66.4	61.2	60.7	55.4
Tin plates and Terne plates	1	1	1	1	1	1	1	72.0	61.9	61.0

[1] Data not available.

[2] None produced by the Steel Corporation.

[3] These are the only secondary products for which data are available.

than these figures indicate. Controlling, as it did, the choicest coking coal lands in the Connellsville region, it was well situated with respect to its supplies of coking coal.

The percentage of the pig iron production of the country controlled by the Steel Corporation remained practically unchanged between 1901 and 1910. In the former year it produced 42.4 per cent of the total; in the latter 43.0 per cent. Here again the figures are for the total production, rather than the production for steel making purposes; and therefore they do not show the real importance of the Steel Corporation in this field. Yet it is evident that the business of the independents increased considerably, since in 1910 they produced about the same percentage as in 1901, despite the acquisition by the Corporation of the Union Steel Company and the Tennessee Coal, Iron and Railroad Company.

Summarizing for the raw materials, it appears that the Steel Corporation held its own fairly well, though its favorable showing resulted in part from the purchase of important competitors.

The best single index as to the Steel Corporation's position in the steel manufacturing industry is the output of ingots and castings. In 1901 the Corporation produced 66.3 per cent of the country's output of these products, but in each succeeding year it lost ground relatively until by 1910 it produced only 54.7 per cent. And this decline came in spite of the purchase of important competitors. To be sure, the Corporation's total output of ingots and castings has increased enormously since 1901. In 1901 it produced only 8,854,820 tons; in 1910, 14,179,369 tons. That the company, despite this growth, did not hold its own is due, of course, to the even more rapid growth of its competitors. While the trust did 60 per cent more business in ingots and castings in 1910 than in 1901, its competitors did 154 per cent more. This, moreover, can not be explained by saying that a large concern finds it more difficult to increase its business at the same rate as its smaller competitors, for the competitors of the Steel Corporation not only grew at a faster rate, but in the aggregate showed an absolute increase in business greater than that secured by the Steel Corporation, including, as the latter

does, the Carnegie Company, easily the most efficient of the steel companies prior to its incorporation in the trust.[1] Though the Steel Corporation was not able to increase its output as rapidly as its competitors, nevertheless it produced vastly more than its nearest competitor in point of size. In 1911 the steel ingot production of the Corporation was 16,856,914 gross tons (55.6 per cent of the country's output), while the largest independent concern—Jones and Laughlin—produced only 1,690,845 tons, or 5.5 per cent.[2]

With respect to the rolled products, taking them as a whole, the Steel Corporation substantially maintained its position. In 1901 it produced 50.1 per cent of the total output of rolled products; in 1910, 48.1 per cent. In individual lines, however, the Steel Corporation lost heavily. In 1901 it produced 62.2 per cent of the structural shapes; in 1910, only 51.3 per cent (the Steel Corporation's output of structural shapes between 1901 and 1910 increased 85 per cent; that of its competitors 188 per cent). In 1901 the Steel Corporation made 64.6 per cent of the plates and sheets; in 1910, only 48.0 per cent (the Steel Corporation increased its output 66 per cent between 1901 and 1910; the independents increased their output 223 per cent). In 1901 the Steel Corporation turned out 77.6 per cent of the wire rods; in 1910, only 67.3 per cent (for the Steel Corporation this represented an increase of 42 per cent; for its competitors, an increase of 139 per cent). In 1901 the Steel Corporation's output of wire nails was 65.8 per cent of the total; in 1910, only 55.4 per cent (between 1901 and 1910 the Corporation's output increased but 9 per cent; that of its competitors, 69 per cent).

The maintenance by the Corporation of its position in rolled products as a whole, despite the decrease in these individual lines, seems to have resulted from an increase in the production of bars, skelp, etc., and from the production in 1908 to 1910 of a large proportion of the open-hearth rails, the Corporation

[1] The Steel Corporation's output of ingots and castings increased between 1901 and 1910 by 5,300,000 tons; that of its competitors by 7,200,000 tons. Report of the Commissioner of Corporations, part I, pp. 360–363.

[2] Brief for the United States (no. 481), vol. I, p. 152.

having produced none at all prior to 1908. With respect to Bessemer rails, the Corporation produced 59.9 per cent of the country's output in 1901, and though there were ups and downs in the years that followed, it produced in 1910 almost exactly the same percentage. In the maintenance of this position the Corporation was greatly aided by its railroad affiliations. In 1911, for example, one or more directors of the Corporation was to be found on the directorate of sixty-two American railroads, possessing a mileage equal to almost half that of the whole country.[1] It would be strange, indeed, if these connections did not bring the Steel Corporation some business which otherwise would have gone to the independent rail manufacturers.

It is evident that the high degree of control which the Steel Corporation had at the time of its organization was being gradually lost. Even in the lines in which it had a quasi-monopolistic position in 1910, it had lost heavily, almost without exception. This decline had taken place, moreover, in spite of the diversity of the businesses into which the influence of the Steel Corporation ramified. From its organization the officers or directors of the company were at various times on the directorate of a vast number of industrial companies. The Steel Corporation's connections with industrial companies and railroads, all large buyers of iron and steel, naturally attracted to it a great deal of business. Furthermore, the Corporation had powerful moneyed connections. At some time after its organization it had directors on as many as eighty-five different banks and trust companies, and twenty-five insurance companies.[2] In addition, according to Mr. Gary, it made a practice of keeping about seventy-five million dollars in cash on deposit in banks.[3] The government in its petition went so far as to charge that the Corporation had built up "a system of interlacing of directorates

[1] Brief for the United States (no. 6214), part II, p. 287.

[2] Ibid.

[3] Senate Report no. 1326, 62nd Cong., 3rd Sess., p. 824. On December 31, 1913, none of the competitors of the Corporation had a capitalization equal to the amount of cash held by the Steel Corporation. Brief for the United States (no. 481), vol. I, p. 138.

which embraced almost the entire commercial and financial powers of the country.[1]

While the fact of the decline in the relative importance of the Steel Corporation is clear, the explanation thereof is not so clear. Possibly those in charge of the Corporation, fearing dissolution proceedings, did not attempt to retain their original degree of control of the steel business of the country. The decision of the Circuit Court refusing to enter a dissolution decree because the Steel Corporation had not been able to hold its own would appear to justify such a policy. On the other hand, not until after 1910 were any of the great trusts dissolved, and it is therefore doubtful whether fear of the law provides the real explanation. Possibly, to give another explanation, the guiding spirits of the Steel Corporation preferred to maintain the prices of iron and steel products,—even at the loss of a proportionate share in the country's growing business,—as a means of squeezing out the water from the company's stock, and of putting it on a more secure foundation. In support of this view it may be said that during periods of industrial depression the proportion of the Corporation's output to the total was generally smaller than its proportion of capacity, owing to its policy of maintaining prices. Thirdly, perhaps the true explanation is the absence of any important economies in the trust form of organization; the sceptic would seem to find here ground for his scepticism.[2]

[1] P. 62.

[2] There is much testimony as to the ability of the Steel Corporation to eliminate its competitors. Most of the witnesses in the government suit agreed that the cost of converting the raw materials into the finished products (conversion cost) was practically the same for the Steel Corporation as for the leading independent concerns. Mr. Donner, president of the Cambria Steel Company, and formerly a director of the American Tin Plate Company, testified that in his opinion the Steel Corporation could not put its competitors out of business "without committing suicide," that if the Corporation were to make prices so low that there was no profit for the Cambria concern, there would be nothing left for the Corporation. (Brief for the United States, no. 481, vol. II, Summary of Evidence, p. 855.) A mill with a capacity of 40,000 to 50,000 tons of ingots per month, if properly designed and operated, ought, he said, to compete with

Even in the absence of important economies, however, a trust might hold its own, could it avail itself of certain props to maintain its position. The Standard Oil Company, as we have seen, found its main strength in certain objectionable features, such as rebates, control of pipe-lines, and unfair selling methods. Had

the Corporation in any of its plants. (Ibid., p. 868.) Mr. Schwab, president of the Bethlehem Steel Company and formerly president of the Corporation itself, testified that the mill cost of the Corporation at Pittsburg or Gary did not differ materially from the mill cost at Bethlehem; that the limit of metallurgical and mechanical possibilities had been reached, and that the conversion cost in all mills throughout the United States was practically uniform. (Ibid., p. 868.) Mr. Corey, formerly president of the Corporation, declared that the cost of production at the Carnegie works was never materially less after the formation of the Corporation than it had been in 1901, at the time the Carnegie works were acquired. (Ibid., p. 869.) Mr. Farrell, then president of the Corporation, enumerated fourteen different steel companies which the Corporation could not put out of business without committing financial suicide. (Ibid., p. 859.) (Whatever may be the verdict with respect to the leading independent concerns, it is much to be doubted, Mr. Farrell to the contrary notwithstanding, whether some of these fourteen companies, such as the Wheeling Steel and Iron Company—with a steel ingot output of less than 1 per cent of that of the Corporation—produced on a large enough scale to compete effectively with the Corporation.) On the other hand, Mr. Campbell, president of the Youngstown Sheet and Tube Company, when asked whether, taking into account the extent of the ore holdings of the Corporation, its ownership of railroads, the extent of its capitalization, the character of men interested in it and their relations to banking circles and railroads, the Corporation had the power to put its competitors out of business, replied, "I think they would have the power; yes, sir . . . I think if Judge Gary would happen to die to-night that there would be a good many steel people that would lie awake until his successor was appointed. (Ibid., pp. 850–851.) Mr. Schwab testified that it cost his company more to make steel rails than it did the Corporation, because his company did not transport its own ore. (Ibid., p. 868.) Judge Gary, the real head of the Steel Corporation, testified in 1908 that the Corporation could produce pig iron cheaper than its competitors; that although the mill costs of production were about the same for the Corporation as for some of the other companies, yet by reason of the control of the best ores the Corporation could undersell them. (Ibid., p. 868.) The conclusion would seem to be that the Corporation by virtue of its ownership of the cream of the ore and coking coal lands and of the iron ore railroads (not to mention its financial connections) had an advantage over its competitors, but that this advantage did not demonstrate the superior economy of the trust form of organization. Rather

the officials of the Steel Corporation been so minded, or did the nature of the business permit, the Steel Corporation might have followed a similar policy. But such has not been the case. In the first place, the Steel Corporation was not the recipient of rebates from the railroads. Mr. James R. Garfield testified in the steel dissolution case that he made an investigation of the relations of the railways to the Steel Corporation similar to the investigation made into the oil business, and he found no evidence of the Steel Corporation having received any rebates.[1] Judge Woolley, of the District Court, stated that there was nothing in the evidence that suggested that the Steel Corporation used its power as a means of securing rebates; on the contrary it appeared that early in its history the Corporation promulgated a rule against soliciting and accepting rebates.[2] The contrast in this respect with the Standard Oil Company is noteworthy. The Steel Corporation, with its iron ore railroads, has not, it is true, lived up to its obligations as a common carrier, but the iron ore railroads cut by no means the same figure in this industry as do the crude oil pipe-lines in the oil industry. Moreover, the Steel Corporation did not endeavor to coerce dealers or consumers into dealing with it exclusively.[3] Neither did it resort to local price cutting as a means of restraining competitive business. Whether it would have done so had circumstances permitted can not be said; the conditions, as a matter of fact, did not permit. On this point the Circuit Court said: "Under conditions incident to the steel trade the power of a large company to carry on a ruinous trade war against any particular competitor does not exist in the iron and steel industry. The customers of the great steel companies are large jobbers and the purchasing agents of other companies, who are in the closest

it demonstrated the many-sidedness of the trust problem and the inability to achieve results in the way of restoring competition except by the adoption of a legislative policy that takes into account the many favoring favors that lie at the basis of the apparent success achieved by some trusts.

[1] Brief for the Steel Corporation (no. 481), p. 119.

[2] 223 Fed. Rep. 171. See also Brief for the Steel Corporation (no. 481), pp. 119–120.

[3] Brief for the Steel Corporation (no. 481), p. 126.

touch with every fluctuation of the steel market. The result is that any effort on the part of any one of these great steel companies to inaugurate a trade war by ruinously underselling a competitor would at once, owing to the sensitiveness and interrelated character of the steel market, result in forcing the company that was thus ruinously selling in any particular market or locality to in the same way ruinously lower its prices in every other community." [1] The Steel Corporation therefore could not wage a localized warfare against its competitors. It could, of course, have reduced the prices of articles made by certain competitors without reducing the prices of the articles not made by these competitors, and in this way have subjected these particular competitors to cutthroat competition. But this policy was not followed. It could also have cut prices to the bone everywhere, yet according to the president of the Cambria Steel Company this would have amounted to an act of suicide. The testimony is ample that the competition of the Steel Corporation, though vigorous, was fair, and conspicuously free from the brutality of which some other trusts have been found guilty.[2] The tariff, it is true, played its part. The iron and steel industry has been a notable recipient of tariff favors, and the combinations and trusts in this industry (notably the tin plate trust) have profited thereby. In fact, some of the trusts of the late nineties would perhaps never have been formed had it not been for the tariff wall, well-nigh insurmountable to foreign competitors. But certainly the tariff was not the mother of the steel trust of 1901; by that time the duty had become nominal. After the removal of the duties from iron and steel products by the Simmons-Underwood bill of 1913, the Steel Corporation for the most part stood on its own feet, unsupported by legislative props,[3] save, of course, such artificial support as was involved in the

[1] 223 Fed. Rep. 77.

[2] On this point, see the testimony of competitors abstracted in the Brief for the Steel Corporation (no. 481), pp. 122–124.

[3] Not all iron and steel products were placed on the free list. Thus, the duty on tubes and pipes was made 20 per cent ad valorem; on tin plate 15 per cent; and on structural shapes 10 per cent. Taussig, Tariff History of the United States (6th edition), p. 441.

failure of the government to prevent the Corporation from acquiring a semi-monopoly of the best iron ore deposits, and from utilizing its iron ore railroads to the detriment of its competitors, —subjects to which we now turn.

In view of the fact that the Steel Corporation was losing its hold on the industry, one might have concluded that the wise public policy would have been that of "watchful waiting," that the steel trust in time would disintegrate by virtue of its very unwieldiness. This may prove to be the outcome, yet it must be remembered that the Steel Corporation is unusually well intrenched in the matter of the essential natural resources. The important elements which go into the manufacture of pig iron (the foundation of the steel manufacture) are iron ore, coking coal, and limestone. Of these the iron ore is the most important, and the Steel Corporation in 1911, when the Report of the Commissioner of Corporations was published, held approximately 75 per cent of all the commercially available iron ore of the Lake Superior district, the ore of this district being the basis of the iron and steel industry of the country.[1] (About 85 per cent of the country's output of iron ore came at that time from the Lake Superior district.) In addition, the Steel Corporation owned immense deposits of iron ore in the South and in other sections, even including deposits in Cuba. Mr. Gary, the chairman of the Steel Corporation, admitted in his testimony before the House Ways and Means Committee in 1908 that the Corporation practically controlled the ultimate ore supply of the country.[2]

The testimony of Mr. Schwab before the Stanley Committee is also significant. Mr. Schwab gave it as his opinion that there would not be any great development in the iron and steel business by new enterprises, because of the difficulty of securing a sufficiently large supply of raw material. Only a concern possessing a large reserve of ore could afford to make the large investment required to produce iron and steel economically, and the

[1] Report of the Commissioner of Corporations, part I, p. 59.

[2] House Document no. 1505, 60th Cong., 2nd Sess., p. 1752.

greater part of the ore on this continent was already owned or leased by existing companies.[1]

The dominating position of the Steel Corporation in the ore industry was heightened through its ownership of iron ore railroads. The Steel Corporation owned the Duluth and Iron Range, and the Duluth, Missabe and Northern, the two most important ore roads in the Lake Superior region.[2] The freight rates charged by these roads were very high, their operating expenses were very low (the operating ratio in 1910 was 36.5 per cent for one and below 30 per cent for the other, against an average of 66 per cent for the whole country); and as a result these ore roads were immensely profitable.[3] In 1911 a considerable reduction in the rates on iron ore was made by the carriers, but, according to the Commissioner of Corporations, they were still excessive.[4] These high rates not only contributed greatly to the enormous earnings of the Steel Corporation, but they imposed a burden on such of its competitors as were obliged to ship their ore over these roads,—for none of the competitors of the Corporation owned any railroads carrying iron ore from the ore fields to the Lake ports. This situation would seem to have called for the application of the principle of the commodity clause; the interests of the public would seem to have required that the Steel Corporation divest itself of its iron ore railroads, and thus remove the inducement which they had to restrain the independent operations by means of excessive freight rates and discrimination in service.

After the report of the Bureau of Corporations was published, the Steel Corporation cancelled the lease it held of the valuable ore lands of the Great Northern Railway system. This lease had been made in 1907 in order to prevent any one else making use of these ore lands (the unusually high rate of royalty leads to

[1] Brief for the United States (no. 6214), part I, p. 390.

[2] These two roads handled about two-thirds of the total ore traffic of the Lake Superior district. Brief for the United States (no. 481), vol. I, pp. 161–162.

[3] Report of the Commissioner of Corporations, part I, pp. 374–375.

[4] Ibid., part III, p. 506. A further reduction was ordered in 1915 by the Interstate Commerce Commission. 33 I. C. C. Reports 541.

this conclusion).[1] It was provided that the lease might be cancelled by the Steel Corporation on January 1, 1915, upon giving two years' notice. On October 17, 1911, the Finance Committee of the Steel Corporation, influenced possibly by the prospect of the filing of a government bill—one was filed on October 26—decided to cancel the lease on January 1, 1915.[2] This action opened up a large supply of excellent ore, which might be made use of by independent operations.

But of more importance as bearing on the ability of the Steel Corporation to effect a monopoly because of a control of the iron ore is the fact that the high class Lake Superior ores owned by the Steel Corporation have become less and less the basis of the steel industry. New fields were developed, and ores which a few years ago were regarded as unusable can now be worked under the improved methods in vogue. The Bethlehem Steel Company, for example, gets its iron ore from the Adirondack mountains in New York, from Sweden, Chili, and Cuba.[3] This company and other tidewater concerns became entirely independent of Lake Superior ore, and after the passage of the Simmons-Underwood bill were not hampered by a duty on foreign ore. The Colorado Fuel and Iron Company has its ore in Wyoming, New Mexico, and Utah; and is also independent of Lake Superior ore. Present indications, therefore, are that the establishment of a trust based on control of the iron ore will prove futile because of new discoveries and improved methods.[4] And such may in other industries frequently prove to be the case. But certainly this will not be true of all industries, and therefore a definite, farsighted policy with respect to our natural resources would seem to be but the part of wisdom.

[1] For an opposing view, see Brief for the Steel Corporation (no. 481), p. 168.

[2] Brief for the United States (no. 6214), part II, pp. 66, 80.

[3] Moreover, new deposits in the Lake Superior district were discovered, thus reducing the Corporation's percentage of the total. See Brief for the Steel Corporation (no. 481), pp. 32–33.

[4] According to the Steel Corporation its ore holdings in the Lake Superior district amount to less than 45.6 per cent of the known and developed ores of the first quality. Brief for the Steel Corporation (no. 481), p. 291.

The foregoing considerations, however, relate to the future. Competition in production continues quite active, and the independents are steadily growing in strength and importance. Yet this competition has not made itself felt fully with respect to prices; competition in prices has been materially restrained by various means,—pools, trade meetings, and dinners.[1] At the time of the organization of the Steel Corporation and for several years thereafter a number of the constituent companies of the Corporation allotted trade and fixed prices by means of pooling agreements.[2] In the year 1904 the president of the Corporation ordered the subsidiaries to withdraw from these pools. Nevertheless shortly thereafter representatives of the same concerns that had been parties to the pools held trade meetings, and at these meetings there were reached understandings with respect to prices by means of which the price level was maintained as effectually as under the agreements.[3] The legality of these meetings was questioned, and in 1907 they were abandoned.[4] They were soon followed, however, by the famous Gary dinners, —another device for substituting coöperation for competition as a regulator of prices.

The first of these dinners was held in New York City on November 20, 1907.[5] The panic of October, 1907, had demoralized the steel trade, and the dinner was held to discuss the proper method of handling the situation. There were present a number of manufacturers of iron and steel, controlling among them at least 90 per cent of the trade.[6] Mr. Gary, in his testimony in the government suit, explained the reason for holding the dinner. "My purpose was . . . to prevent the demoralization of business, to maintain so far as practicable the stability of business

[1] Tables showing the prices of iron and steel products from 1895–1913 may be found in Brief for the United States (no. 481), vol. II, pp. 1037–1085.

[2] 223 Fed. Rep. 173. See also Brief for the Steel Corporation (no. 481), p. 208.

[3] 223 Fed. Rep. 173.

[4] Ibid. According to the Brief for the Steel Corporation (no. 481), p. 219, they were abandoned in October, 1906.

[5] Brief for the United States (no. 6214), part II, p. 146.

[6] Ibid., p. 147.

and to prevent, if I could, not by agreement, but by exhortation, the wide and sudden fluctuation of prices which would be injurious to everyone interested in the business of the iron and steel manufacturers." [1]

This "exhortation" to his fellow-manufacturers was supported by an elaborate scheme for controlling prices. As a result of the dinner a general Advisory Committee of five members was appointed, Mr. Gary being chairman.[2] This committee was empowered to appoint sub-committees; and it did appoint nine such committees, one on ore and pig iron, another on rails and billets, and so on. The Steel Corporation was well represented on these committees, having two representatives on the General Committee, and one representative on each of the nine sub-committees.[3] The sub-committees held meetings in various parts of the country with more or less regularity for several months. The president of the Youngstown Sheet and Tube Company was made a member of the sub-committee on sheets and plates. He testified in the government suit that shortly after the dinner of November 20, 1907, he attended a meeting in Pittsburg of the manufacturers of tin plate and sheet steel, at which there were present 90 per cent of the manufacturers of sheet steel; that this meeting was an outgrowth of the first Gary dinner; and that at this meeting each manufacturer was questioned in regard to his percentage of the business, and his mill operations.[4] When the maintenance of the market prices was discussed, what was in mind was the prices published by the subsidiaries of the Steel Corporation. He further testified that, when he was chairman of a sub-committee meeting, he would ask those present to state whether they thought the price was too high, or whether it was too low, and that, when a consensus of opinion had been reached, he would call on each one to state what policy he would follow with respect to prices.[5] He made it clear to the members that agreements were illegal; and that there would be no agreement, no penalties, and no restriction of out-

[1] Brief for the United States (no. 6214), part II, p. 149.
[2] Ibid., p. 147.
[3] Ibid., p 150.
[4] Ibid., p. 151.
[5] Ibid., p. 152.

put. But in response to inquiry from the government examiner he stated that he thought that there was a general understanding "that their policy would be to market their product at the then prevailing price until they notified their competitors that they wanted to change their price." [1] The witness also attended the meetings of the tube manufacturers and of the manufacturers of billets and sheet bars, and they were conducted on substantially the same basis. The president of the McKeesport Tin Plate Company admitted that the effect of the meetings was to maintain a steady price, and that after prices were announced he would feel under a moral obligation to sell at that price until he notified his competitors of an intention to change.[2] Much additional testimony might be cited; but the following excerpt from the testimony of the president of the Steel Corporation from 1903 to December 31, 1910, will suffice:

"Q. State whether or not it was the purpose, in the creation of these sub-committees to reach a general understanding as to prices of iron and steel products and to bring about the maintenance of them.

The Witness. Yes.

Q. Were there understandings as to what those prices would be?

The Witness. There were.

Q. Were the prices maintained or not as a result of those understandings?

The Witness. They were." [3]

It seems clear that through the General Committee and the sub-committees the manufacturers of steel coöperated, not only in maintaining the market price, but also in making the market price identical with that quoted by the subsidiaries of the Steel Corporation.

In February, 1909, this policy of coöperation was temporarily abandoned. Business had so declined in volume that the independents refused to abide by the "understandings," and sold at

[1] Brief for the United States (no. 6214), part II, p. 153.

[2] Ibid., p. 168.

[3] Ibid., pp. 168–169.

prices determined by themselves.[1] The Steel Corporation attempted for a time to maintain prices by itself, but soon abandoned the attempt, and established an open market in steel products, except in rails.[2] In October, 1909, the meetings of the steel manufacturers at luncheons and dinners were resumed, and the result was the restoration of the policy of coöperation.[3] In the fall of 1910 and the early part of 1911 there were further meetings of the officials of the Steel Corporation with the other steel manufacturers.

Fortunately the speeches made at the dinner of January 11, 1911, have been preserved, and these clearly show the workings of the Gary dinners. In his speech Mr. Gary said in part:

"We have something better to guide and control us in our business methods than a contract which depends upon written or verbal promises with a penalty attached. We, as men, as gentlemen, as friends, as neighbors, having been in close communication and contact during the last few years, have reached a point where we entertain for one another respect and affectionate regard. We have reached a position so high in our lines of activity that we are bound to protect one another; and when a man reaches a position where his honor is at stake, where even more than life itself is concerned, where he can not act or fail to act except with a distinct and clear understanding that his honor is involved, then he has reached a position that is more binding on him than any written or verbal contract." [4]

In his speech Mr. Gary further said that in his opinion it would be a mistake to reduce prices at that time. At this same dinner a representative of Jones and Laughlin said in part, "I hope it will be the consensus of opinion here to-night that we will maintain the present prices." [5] The president of the Ashland Steel Company said that so far as his company was concerned, "we are ready and willing to still coöperate to do what we can to

[1] 223 Fed. Rep. 175.
[2] Brief for the United States (no. 6214), part II, p. 200.
[3] Ibid., p. 207.
[4] Ibid., (no. 481), vol. II, pp. 989–990.
[5] Ibid., p. 993.

maintain prices."[1] Mr. Gary, during the course of the dinner, called on practically all of the leading steel manufacturers, and each, almost without exception, expressed himself as in favor of maintaining the existing prices, or as ready to support the coöperative movement with respect to prices.

Whether as a result of the investigation of the Stanley Committee of the House of Representatives or in anticipation of the government suit, the Gary dinners came to an end in 1911, and judging from the movement of prices, the coöperative arrangement was given up. With respect to these dinners the Stanley Committee said:

"We think the conclusion is irresistible that the Gary dinners were instituted as a means of conveying to the entire iron and steel industry information as to what the attitude of the United States Steel Corporation was upon the questions of output and prices and of impressing upon all engaged in the industry that it was the part of wisdom and prudence to govern themselves accordingly. We further believe that by this means prices were maintained, output restricted, competition stifled, and trade restrained, just as certainly, just as effectively, and just as unlawfully as had been done under the discarded pooling agreements of former years."[2]

Perhaps the best evidence of the success of the policy of coöperation, promoted by pools and dinners, is the course of the price of Bessemer steel rails. From 1867 to 1900 (the year before the formation of the steel trust) the price of steel rails varied every year; in no two years during all this period did it continue the same.[3] Prior to the formation of the Steel Corporation there was severe competition in steel rails, and the price fell from $28 per ton in 1896 to $17 per ton in 1898. A combination then raised the price for a time to $35, but early in 1901 it went as low as $26. In April, 1901, the Steel Corporation began operations; in May the price of rails was fixed at $28 per ton; and the price remained at that figure up to the date of the government suit,

[1] Brief for the United States (no. 481), vol. II, p. 998.

[2] Stanley Committee Report, p. 126.

[3] Brief for the United States (no. 6214), part I, p. 13.

having been effectively controlled by the Steel Corporation in coöperation with the independent steel manufacturers. This price of $28, it may be noted, was some $10 per ton higher than the prices that prevailed during 1897–1898, when there was competition between the Carnegie Steel Company and the Illinois Steel Company; though the prices of 1897–1898 yielded these companies a substantial profit.[1] The ability of the Steel Corporation to maintain the price of steel rails at an arbitrary figure, despite marked fluctuations in demand [2] and in manufacturing costs, abundantly testifies to the tremendous power of this mammoth organization.

[1] Brief for the United States (no. 481), vol. I, p. 169.

[2] In 1901, 99.9 per cent of the rails sold were Bessemer rails. Since than date Bessemer rails have been largely superseded by open-hearth rails. In 1912 only one-third of the rails sold were Bessemer rails. Brief for the Steel Corporation (no. 481), p. 215.

CHAPTER X

THE INTERNATIONAL HARVESTER COMPANY [1]

The International Harvester Company—the harvester trust—was organized in New Jersey on August 12, 1902. It represented a consolidation of the five leading manufacturers of harvesting machines,—the McCormick Harvesting Machine Company (with a factory at Chicago), the Deering Harvester Company (with a factory at Chicago), the Warder, Bushnell and Glessner Company (with a factory at Springfield, Ohio), the Plano Manufacturing Company with a factory at Plano, Illinois (near Chicago), and the Milwaukee Harvester Company (with a factory at Milwaukee).[2] The five plants of these companies, according to an official statement, were the largest and most complete of their kind in the world.[3] Among them they produced approximately 85 per cent of the total output of harvesting machines in the United States.[4] Their control of the harvester trade in the territory adjacent to them (the great grain growing states of the country) was even greater than 85 per cent, since the leading competitors of the trust were located in New York

[1] On the International Harvester Company see: Report of the Commissioner of Corporations on the International Harvester Company, March 3, 1913; Report of the Federal Trade Commission on the Causes of High Prices of Farm Implements, May 4, 1920; Brief for the United States in International Harvester Company *v.* United States (no. 757); Brief for the International Harvester Company (no. 757); Brief for the United States in International Harvester Company *v.* United States (no. 56); Brief for the International Harvester Company (no. 56); Appendix to defendant's brief in United States *v.* International Harvester Company (no. 624); 237 Missouri Reports 369–424; 234 U. S. 199–215; 214 Fed. Rep. 987–1012.

[2] Report of the Commissioner of Corporations on the International Harvester Company, p. 67. Hereafter referred to as Report on the International Harvester Company.

[3] Chron., 75, p. 345 (August 16, 1902).

[4] Report on the International Harvester Company, p. 67.

state, with a market largely confined to the North Atlantic states and to foreign countries.

Prior to the organization of the International Harvester Company competitive conditions had prevailed in the manufacture of harvesting machines. Notable improvements in the manufacturing processes, combined with a steady increase in the size of the factories, had led to marked economies in production; and these in turn, owing to competition, had led to considerable price reductions. At various periods during the eighties the manufacturers had endeavored, through price agreements, to hold competition in check, but without marked success. In 1887 and again in 1890 attempts had been made to form a combination of the leading manufacturers, and in 1890 a company had actually been chartered for that purpose; but in both instances the plan had fallen through. From 1890 until the organization of the International Harvester Company in 1902 apparently no attempt had been made to effect a consolidation. Competition, generally speaking, had been quite active. In fact the organizers of the International Harvester Company subsequently claimed that it was the severity of competition that made a combination necessary. The president of the International Harvester Company characterized the competition as fierce; list prices could not be maintained.[1] Mr. Glessner, of Warder, Bushnell and Glessner, expressed the opinion that "in the harvester business there was a competition never known in any other business in the world."[2] Mr. Jones, of the Plano Manufacturing Company, testified that competition was so severe that neither the manufacturers nor the dealers were making anything.[3] Moreover, the Commissioner who heard the testimony in a suit in a Missouri court described the competition as "active, persistent, strenuous, and fierce."[4]

The claim that the formation of a harvester trust was necessary to avoid ruinous competition was analyzed by the Bureau of

[1] Report on the International Harvester Company, p. 59.
[2] Ibid., p. 60.
[3] Ibid., p. 61.
[4] 237 Missouri Reports 384.

Corporations in its investigation of the International Harvester Company. "There is no doubt" said the Bureau, "that the principal motive for the formation of the International Harvester Co. was to eliminate competition and to secure a dominant position in the trade." [1] Though the desire to eliminate competition led to the organization of the trust, yet competition was not so severe, in the opinion of the Bureau, as to make the formation of a trust necessary. Most of the larger companies, it reported, had been making considerable profits, and sometimes very large profits.[2] Specific information as to the profits of the harvester companies prior to 1902 was difficult to obtain, and such data as was gathered by the Bureau related only to the five companies which united to form the trust. But these five companies, as has been pointed out, included the five leading manufacturers, and produced over four-fifths of the total output. Such data as was available showed that in general the profits of the large companies had been quite high during the five years preceding the organization of the International Harvester Company. The Plano Manufacturing Company, it is true, had sustained a deficit in both 1900 and 1901, and the profits of the Milwaukee Company had been low in 1901; but the profits of the McCormick and Deering companies had been high in every one of the five years, and the profits of the Milwaukee Company and of Warder, Bushnell and Glessner (the Champion Company) had generally been high.[3] It is significant that in three of the five years for which the profits were shown the aggregate annual profit of the five competing companies was greater than the reported profit of the trust during any one of the first six years of its existence, and this notwithstanding the fact that the period after 1902 was one of great prosperity.[4] It is also significant that a committee appointed to consider the taking over of

[1] Report on the International Harvester Company, p. 70.

[2] Ibid., p. 62.

[3] Ibid., p. 63.

[4] Ibid., p. 64. A possible explanation of the low "reported" profit of the trust is the large amount of earnings put back into the business, especially in new lines and in plants abroad.

the business of the five companies which combined to form the trust reported that each of these companies had for several years enjoyed a "prosperous, profitable and growing business." [1] In addition, the McCormick and Deering companies, especially, had been increasing their business rapidly prior to the merger.[2] The Bureau by way of conclusion said: "This large increase in the volume of business taken in connection with the comparatively high rates of profits earned on the capital invested is strong evidence of the fact that the companies which originally formed the International Harvester Co. were generally not suffering from excessive competition. The combination, therefore, can not be justified on the principle of self-preservation." [3]

The argument most frequently advanced in favor of trusts is that they make possible economies not otherwise realizable. But—so the Bureau of Corporations claims—the expectation of reducing costs was only a secondary motive in the organization of the harvester trust.[4] This matter will be considered in more detail later on in this chapter, but at this point it may be stated that the International Company did effect a high degree of integration. Through its constituent companies it acquired coal lands, iron ore properties, iron and steel plants, timber lands, and saw mills. By supplying itself with its chief raw materials at cost, the company not only had an assured supply, but kept for itself the profits that otherwise would have gone to other concerns. (This assumes that the company could produce its steel, for example, cheaper than it could buy it from the steel trust, an assumption apparently justified in view of the fact that the company continued to make its own steel.) With the manufacturing properties also went binder twine mills and several industrial railroads. The McCormick concern owned the

[1] Brief for the United States (no. 56), pp. 18–19.

[2] Between 1899 and 1902 the assets of the McCormick Company increased from $12 million to $50 million, all from earnings. Its sales of the principal harvesting machines increased from 371,312 in 1900 to 503,517 in 1902; and the Deering Company's sales increased during the same period from 281,574 to 370,107. Brief for the United States (no. 56), p. 8.

[3] Report on the International Harvester Company, p. 66.

[4] Ibid., p. 70.

Illinois Northern Railway, a short line connecting the McCormick plant and other industrial enterprises with several railroads entering Chicago; and the Plano concern owned the Chicago, West Pullman and Southern Railway.

Another motive in the organization of the International Harvester Company was the promotion of the export trade in agricultural implements. It was claimed on behalf of the company that none of the companies then in the business had sufficient capital and credit to develop the foreign trade adequately, or had sufficient trained harvester men to create an organization that would effectively cover the foreign field.[1] The foreign trade argument, it may be noted, is often cited as a justification for the trust. Just what importance this factor played here is hard to say. The testimony of the president of the International Harvester Company shows that the five companies that entered the trust had already built up a very large export business; and this was true, also, of the four independent harvester companies in New York state.[2] As a matter of fact, American harvesting machines were then being marketed all over the world. After the International Harvester Company was organized, the foreign trade, it is true, was much extended, yet whether this resulted from the organization of the trust or whether it would have come about anyhow is something on which it is difficult to pass judgment—is, in the words of Judge Smith, "a mere matter of speculation."[3]

Still another motive for the formation of trusts is the profit obtained by the promoters.[4] The bankers who promoted the harvester trust received $3,148,197 in stock for the Milwaukee Harvester Company,—one of the five original companies. This sum seems to have represented the value of the property conveyed. In addition they received $2,957,143 in stock for their services as promoters, this sum being over and above all expenses

[1] Brief for the International Harvester Company (no. 56), pp. 55–56. See also p. 525.

[2] Report on the International Harvester Company, pp. 71–72.

[3] 214 Fed. Rep. 993.

[4] Cf. pp. 293 seq.

incurred in the formation of the Harvester Company. This payment of almost $3,000,000, in the opinion of the Bureau of Corporations, was excessive. To the extent that it was excessive it served as an inducement for the promoters to form the trust. But undoubtedly it would be a mistake to attach much importance to this factor in endeavoring to explain the organization of the International Harvester Company.

The formation of the International Harvester Company was noteworthy for the absence of any important overcapitalization. At its organization the company had a capital of $120,000,000, all common stock (no bonds). Without going into the financial details of the promotion, half of the stock ($60,000,000) was issued for cash, which was to constitute working capital; and the other half was issued for the properties acquired and for bankers' commissions.[1] Whether there was any overcapitalization depended therefore on whether the properties acquired were worth $60,000,000. The organizers appraised the value of the property at approximately $67,000,000, not counting good will, and the company claimed, therefore, that it commenced operations with a surplus of $7,000,000.[2] The Bureau, however, regarded the appraisal value as excessive. Though it found it difficult to arrive at an accurate valuation because of the fact that the records of the company were not well kept, and because in some instances the company denied access to the records, nevertheless the Bureau felt that a fair valuation would be about $49,000,000, not including the good will.[3] In the opinion of the Bureau, the difference between $60,000,000 and $49,000,000 must be regarded as having been issued for good will and promotion services. But there can be no doubt that a substantial amount of good will was brought into the merger, quite apart from any so-called merger value. It follows, therefore, that if the International Harvester Company was overcapitalized, it

[1] Report on the International Harvester Company, p. 86.

[2] Ibid., p. 95. See also Report of the International Harvester Company for 1907, in Chron., 86, pp. 1471–1474.

[3] Report on the International Harvester Company, pp. 94, 96, 125.

was only to a slight degree. This variation from the customary practice is perhaps to be explained partly by the stock market conditions in 1902, and partly by the fact that the constituent companies were for the most part close corporations. The McCormick family alone received 42.6 per cent of the stock of the International Company, and the Deering family received 34.4 per cent. These two groups between them, therefore, received 77 per cent of the total capitalization, and were thus in full control.

After its organization the International Harvester Company acquired a number of competing enterprises. In 1903 it purchased D. M. Osborne and Company, the leading independent concern.[1] This company had its plant at Auburn, New York, and was thus in a favorable position to compete for the export trade. Its chief product was harvesting machines, but it also manufactured tillage implements and binder twine. As part of the terms of the sale the two leading active stockholders of the Osborne concern agreed that for a period of ten years they would not engage in the business in the United States (except in Arizona and New Mexico), Europe (except Belgium and Holland), South America, or Australia, thus evidencing the monopolistic purpose of the International Harvester Company. During 1903 and 1904 the purchase of the Osborne concern was kept secret. This was at the request of the Osborne Company, in order to enable it to collect its bills receivable.[2] During this period an official of the Osborne Company made affidavits, as required by the anti-trust laws of the state of Missouri, that the company was not a party to any agreement or combination to fix prices or output, and that it had not entered into any arrangement which in any way tended to interfere with full and free competition in the manufacture and sale of its products.[3]

During 1903–1904 some of the stockholders of the International Harvester Company acquired the Minnie Harvester Company, the Aultmann-Miller Company, and the Keystone

[1] Report on the International Harvester Company, p. 137.
[2] Brief for the International Harvester Company (no. 757), p. 38.
[3] Report on the International Harvester Company, p. 296.

Company. These three companies were competitors of the International Company, and were acquired—the Bureau believed—largely, if not almost wholly, for the purpose of eliminating their competition.[1] In each case the control was kept secret, and the companies passed as independents. In 1905 these three companies (and the Osborne Company) were transferred to the International Company, apparently as the result of a change of policy on the part of the management. Thereupon the production of binders at these three plants was discontinued, and the plants were used to manufacture binder twine, auto buggies, trucks, and other lines.

The International Harvester Company also endeavored to extend its control to other lines of farm machinery,—lines not competing with harvesting machines. In 1904 some of the stockholders of the company secured control of the Weber Wagon Company; and in 1905 the property of this company was transferred to the International. The Weber concern occupied a very important position in the farm wagon trade; and through it and the later extension of its business the International Harvester Company became one of the leaders in this line.

In 1906 the International Company acquired a manure spreader plant, and subsequently it attained a commanding position in this branch also. The company, in addition, became the selling agent for a number of concerns making plows, seeding machines, etc., and in this way broadened its interest in the farm machinery trade.

The company also developed the new lines at its old plants. Thus, at the Milwaukee plant the manufacture of gasoline engines, cream separators, and tractors was begun in 1904, 1905, and 1909, respectively. The brands formerly made at the Milwaukee plant were thereafter made at the McCormick works. Likewise the Plano plant ceased manufacturing harvesters—the brands formerly turned out there were thenceforth manufactured at the Deering plant—and in 1905 and 1906 commenced the manufacture of manure spreaders and wagons. The Champion plant continued to make harvesting machines, but it added

[1] Report on the International Harvester Company, p. 141.

hay tools in 1903, seeders in 1906, and manure spreaders in 1908. In 1910 a large tractor works was opened in Chicago. This was the only important new plant for the manufacture of agricultural implements constructed by the company in the United States.

From the sales end this extension into new lines was quite advantageous. The sales of harvesting machines in any given territory are generally made within a comparatively short period in each year. The sales force in the past had been employed for only a few months during each year, and it had then been disbanded.[1] The extension of the business to include agricultural implements used at different seasons of the year made it possible to sustain an all-year-round selling organization, thus contributing decidedly to its efficiency.

The Harvester Company also strengthened its position in the export trade. This it did by the purchase of foreign companies, or by the construction of plants abroad. For example, in 1903 the International Harvester Company of Canada was incorporated. It built a large harvester factory at Hamilton, Ontario, and subsequently added tillage implements, seeders, and manure spreaders. Other smaller plants were likewise acquired in Canada. The Harvester Company also built or acquired plants in France, Germany, Russia, and Sweden, and organized marketing companies in a number of other countries. The establishment of these factories abroad was chiefly the result of the protective policy of these foreign countries. Generally speaking, it proved more profitable for the International Harvester Company to manufacture the machines abroad (thus saving the tariff duty) than to make them in this country and export them. Obviously there was a great saving in transportation charges as well, though this saving was offset in part, at least, by the greater cost of production in the foreign plants, the industry being one particularly suitable to this country, and one in which the economies of large-scale production are great.

In 1913 there was made an important reorganization directly affecting the newly acquired lines and the foreign business. On

[1] Brief for the International Harvester Company (no. 757), p. 61.

account of the suit brought by the government to effect the dissolution of the International Harvester Company on the ground that it was a combination in restraint of trade, the board of directors organized in the state of New Jersey on January 27 a new company, called the International Harvester Corporation.[1] To the Corporation were transferred all the domestic plants exclusively engaged in the manufacture of the "new lines," all the foreign plants, and all the transportation companies.[2] The capitalization of the Corporation consisted of $30,000,000 preferred stock and $40,000,000 common. This, it may be noted, represented just half the total of each class of stock of the International Harvester *Company*. The Company, starting out with a capital of $120,000,000, all common, had in 1907 converted half of the common into preferred. In 1910 it had declared a 33 1/3 per cent common stock dividend, thus increasing its total capitalization to $140,000,000. Because of the organization of the *Corporation* with a capital of $70,000,000, the Company reduced its capital from $140,000,000 to $70,000,000, and changed its name to the International Harvester Company *of New Jersey*.[3]

This plan of dissolution was approved by the stockholders in February, 1913. Of this plan the Bureau said: "If intended as a part of a proposed plan of disintegration, the Bureau regards this method of division as very unsatisfactory. Obviously, it does not touch the most essential feature of the company as a combination of competitors, namely, the consolidation of the chief harvesting-machine plants of the country, and especially of the McCormick, Deering, Champion, and Osborne works."[4]

In this connection mention may be made of another company, which is liable to be confused with one or the other of the foregoing companies. This is the International Harvester Com-

[1] Chron., 96, p. 365 (February 1, 1913).

[2] Report on the International Harvester Company, pp. 169, 174.

[3] Holders of the $70,000,000 cancelled stock were entitled to receive cash ($100 per share) or shares in the corresponding class of security of the Corporation.

[4] Report on the International Harvester Company, p. 178.

pany *of America*. In the original merger the International Harvester Company did not acquire the stocks of the companies combined; it merely acquired their properties. But a few weeks later it did acquire the capital stock of the Milwaukee Harvester Company, and with it its charter.[1] The stock of this company, as distinguished from its factory (which had already been acquired), was secured in order that the company might be employed as a selling agency, and thus relieve the International Harvester Company of the restrictions that it was likely to meet in the conduct of business in other states. Thus, the laws of some states excluded corporations with a capital as large as that of the International Harvester Company, and the laws of others, while admitting foreign corporations (that is, corporations chartered outside the state), subjected them to heavy taxation, and sometimes, if they were trusts, refused to license them. The International Harvester Company, being a new corporation, would doubtless have experienced some delay in securing licenses in the several states; it might have been denied a license in others on the ground that it was a trust; and it would probably have been subject to heavy taxation, since the laws of some states made the amount of capitalization the basis of taxation. The Milwaukee Harvester Company, however, already had licenses to do business in the several states, and it was thus well suited to serve as a selling agency. The International Harvester Company, therefore, transferred to the Milwaukee Harvester Company (the name of which was changed in September, 1902, to the International Harvester Company of America) practically all of its warehouses and other facilities for the sale of its machines, and constituted it its sole selling agent.[2] The International Harvester Company (of New Jersey), through the ownership of all of the capital stock of the International Harvester Company of America, of course controlled its selling agent completely.[3]

[1] Report on the International Harvester Company, p. 87.

[2] Ibid., p. 90, and 237 Missouri Reports 383.

[3] The use of the International Harvester Company of America as a selling agency was held by the Supreme Court of Missouri to be in violation of the

The International Harvester Company at its organization produced, as we have seen, about 85 per cent of the country's output of harvesting machines. This figure is not exact, since the number of each type of harvesting machines produced by the independent concerns is not known. However, reasonably complete data for grain binders, mowers, and rakes—three of the most important machines—are available, and especially for the first two. We may therefore turn to an examination of the position of the International Harvester Company in these leading branches of the industry.

The number of each of these machines sold in 1902 by the trust and by the independents, with percentages, is shown in the following table.[1]

	International Harvester Co		*Independent concerns*	
	No. sold [2]	*Per cent*	*No. sold* [3]	*Per cent*
Grain binders	180,024	90.9	18,128	9.1
Mowers	297,880	81.2	68,890	18.8
Rakes	165,219	67.0	81,376 [4]	33.0

The trust, it appears, sold over ninety per cent of the binders, over eighty per cent of the mowers, and nearly seventy per cent of the rakes. These figures, it should be noted, are for the total sales of each group, including the export trade. Inasmuch as the independent binder concerns had a relatively large export trade, the International Harvester Company undoubtedly controlled a larger percentage of the domestic market than the figure for

state law forbidding a company with a capital as large as that of the International Harvester Company to obtain a license, and a fine and ouster (suspended conditionally), was ordered. 237 Missouri Reports 374, 398. This decree was affirmed by the Supreme Court of the United States. 234 U. S. 215.

[1] Report on the International Harvester Company, p. 92.

[2] Number produced in the case of the Milwaukee Harvester Company.

[3] Number produced in the case of the Osborne Company.

[4] Number for independents partly estimated.

total sales (90.9 per cent) would indicate. The same is true to a lesser degree of mowers also.

Similar statistics are not available for reapers or corn binders—other important types of harvesting machines—yet in all probability the proportion of the business in these lines controlled by the International Harvester Company was nearly as great as the figure shown above for grain binders.

Always pertinent is an examination of the ability of a trust, once formed, to retain its monopolistic position. Sufficient data are available to indicate with substantial accuracy the relative position of the International Company and the independents in the leading lines from 1902 to 1911 and in 1918. The situation with respect to grain binders is shown in the table below.[1]

PRODUCTION OF GRAIN BINDERS IN THE UNITED STATES, 1902–1911, 1918

	International Harvester Co.		*Independents* [2]	
	Number	*Per cent*	*Number*	*Per cent*
1902	180,401 [3]	90.9	18,128	9.1
1903	184,817	94.2	11,448	5.8
1904	87,371	89.1	10,649	10.9
1905	102,832	90.0	11,469	10.0
1906	108,666	87.0	16,233	13.0
1907	117,854	88.5	15,264	11.5
1908	104,547	89.7	12,054	10.3
1909	100,204	87.1	14,848	12.9
1910	125,382	87.0	18,701	13.0
1911	146,981	87.0	21,923	13.0
1918	53,281	65.3	28,312	34.7

[1] Report on the International Harvester Company, p. 180; and Report of the Federal Trade Commission on the Causes of High Prices of Farm Implements, p. 679.

[2] Output of the five companies entering the trust in 1902.

[3] When the number produced by the independents was not known, the number sold was used instead. As a rule it made little difference which figure was used.

From an examination of this table it appears that the International Harvester Company increased its proportion of the output of binders from 90.9 per cent in 1902 to 94.2 per cent in 1903. This may be ascribed chiefly to the acquisition in 1903 of the important Osborne concern. Beginning in 1903 there was a decline, until in 1906 only 87.0 per cent of the output was produced by the trust. After a slight increase in 1907 and 1908 the percentage declined again in 1909 to 87, where it remained in 1910 and 1911. The International Harvester Company, therefore, in spite of the acquisition of several competitors, did not quite hold its own. Moreover, it is significant that while the total output of the independents increased between 1902 and 1911, notwithstanding the acquisition of several of their number by the Harvester Company, the total output of the trust actually declined. Nevertheless the International Company still had in 1911 a monopoly position in the manufacture of binders. Between 1911 and 1918, however, the company lost heavily. Whereas in 1911 it had produced 87 per cent of the total output, by 1918 its percentage had fallen to 65.3 per cent.[1] This marked decline was partly due to the growth of some of its competitors, and partly due to the falling off in 1918 of the export trade, in which the International Harvester Company was the leading factor.

The situation with respect to mowers is shown in the table on page 245.[2]

As with binders, the International Harvester Company, through the acquisition of the Osborne concern, increased its proportion of the country's output of mowers in the year after its organization. In 1902 the company produced 82.5 per cent of the mowers produced in this country; in 1903, 87.7 per cent. Yet its proportion since 1903 has shown a declining tendency. In 1911 it amounted to 76.6 per cent, and in 1918 to only 59.5 per

[1] Report of the Federal Trade Commission on the Causes of High Prices of Farm Implements, p. 679.

[2] Report on the International Harvester Company, p. 182; and Report of the Federal Trade Commission on the Causes of High Prices of Farm Implements, p. 679.

PRODUCTION OF MOWERS IN THE UNITED STATES, 1902–1911, 1918

	International Harvester Co.		*Independents* [1]	
	Number	*Per cent*	*Number*	*Per cent*
1902.....	324,180 [2]	82.5	68,913	17.5
1903.....	318,505	87.7	44,755	12.3
1904.....	221,186	82.1	48,309	17.9
1905.....	250,677	84.1	47,468	15.9
1906.....	213,269	79.0	56,860	21.0
1907.....	260,764	81.6	58,730	18.4
1908.....	276,349	82.1	60,467	17.9
1909.....	279,589	80.7	66,970	19.3
1910.....	260,526	77.7	74,630	22.3
1911.....	241,285	76.6	73,886	23.4
1918.....	111,501	59.5	75,809	40.5

cent. Whereas the output of mowers by the independents increased nearly 7,000 between 1902 and 1918, that of the trust declined by over 210,000.

The data for rakes are not so complete. The Bureau estimated, however, that the five companies merged into the International Harvester Company produced in 1902, 67.8 per cent of the rakes; that in 1903, with the acquisition of the Osborne Company, the proportion probably exceeded 80 per cent; and that in 1911 it had fallen to about 72 per cent.[3] The percentage in 1918 was placed by the Federal Trade Commission at 57.5.[4]

The dominant position of the International Harvester Company is well brought out by the following table, which shows the number of harvesting machines of all kinds sold in 1911 by every

[1] When the number produced by the independents was not known, the number sold was used.

[2] Output of the five companies entering the trust in 1902.

[3] Report on the International Harvester Company, p. 183. According to the Brief for the International Harvester Company (no. 56), p. 108a, the International Company in 1905 sold 77.8 per cent of the rakes disposed of in this country, and in 1911, 67.8 per cent.

[4] Report on the Causes of High Prices of Farm Implements, p. 679.

concern contributing as much as 1 per cent to the country's total sales, and the percentage sold by each.[1]

SALES OF HARVESTING MACHINES IN THE UNITED STATES IN 1911, WITH PERCENTAGES

	Number	*Per cent*
International Harvester Co	374,390	76.96
Acme Harvesting Machine Co	23,603	4.85
Johnston Harvester Co	18,684	3.84
Deere and Co	16,886	3.47
Emerson-Brantingham Co	14,480	2.98
W. A. Wood Mowing and Reaping Machine Co	13,017	2.67
Adriance, Platt and Co	8,193	1.69
Thomas Mfg. Co	5,800	1.19

The International Harvester Company in 1911 sold over three-fourths of the total number of harvesting machines sold in this country. Its percentage would be even larger were it calculated upon a basis of value rather than of number, since the company's control, generally speaking, was greatest for the higher priced machines, such as grain binders, corn binders, and headers. The next largest harvester concern was the Acme Company, with a capital of $3,500,000 (the capital of the International Company was $70,000,000).[2] The Acme Company sold less than 5 per cent of the harvesting machines sold in this country, and unlike the International it did not make the entire line of harvesting machines. The only independent concern that did make an entire line was the Johnston Harvester Company, capitalized at less than $2,000,000, and producing less than 4 per cent of the total output of harvesting machines. In corn binders the International Company in 1911 had only three competitors; in reapers, only four; and in grain binders, eight, four of whom were quite unimportant. In mowers and rakes alone was there any considerable number of competitors; but none of them had as much as 8 per cent of the trade in either of these lines.[3] Again, hardly any of the independents competed

[1] Brief for the United States (no. 56), p. 26.
[2] Ibid., p. 111.
[3] Ibid., p. 110.

with the International Company throughout the whole United States; their sales were confined mainly to the East, especially New York state and the New England states.

Since the above date (1911) a number of strong concerns have entered the field. Among them is Deere and Company, with a capital in 1911 of $58,007,100. This expansion of the Deere Company was made on the principle of carrying a full line (no company, not even the International, had a really complete line of farm machinery),[1] and the strong selling organization already possessed by the Deere Company and by other independents made it easier for them to secure a good share of the harvesting machine business than it would have been for a newly organized concern.

So far as the lines other than harvesting machines are concerned, the Bureau of Corporations estimated that the International Harvester Company produced in 1909 the following percentages of the various products.[2]

Corn shredders	55.7
Binder twine	55.1 (62.7 in 1911)
Manure spreaders	55.1 (1911)
Spring tooth harrows	49.1
Disk harrows	25.9 (43.1 in 1911)
Hay stackers	24.2
Hay loaders	20.8
Farm wagons	13.0 (about 15.0 in 1911)
Wheeled cultivators	11.5

Through the acquisition of other companies and through the expansion of its own plants, the International greatly increased its output in the new lines. Naturally its monopolistic position in the harvesting machine trade facilitated this development of its business.

How is the ability of the International Harvester Company to

[1] The acquisition of plow plants by the International Harvester Company in 1919 has given it practically a full line, since plows were practically the only type of farm implement it was not then producing.

[2] Report on the International Harvester Company, pp. 184–188. The estimate is based on the Census reports and the production of the International Company as given in its annual reports.

maintain its semi-monopolistic position to be explained? The chief sources of its power seem to have been two: first, its productive efficiency; second, its possession of large financial resources.

First. The International Harvester Company, generally speaking, produced its machines at a lower cost than its competitors. This was especially true of grain binders, the most important harvesting machine. Thus, the average factory cost of producing binders at the domestic plants of the International Harvester Company during the two years 1910 and 1911 combined was $56.32, the figures for the different plants being $54.11, $56.30, $64.94 and $73.78.[1] (These factory costs do not include general and miscellaneous expenses, nor a very large item of selling expense.) The average factory cost for the four leading independents was $70.83. (To some extent these differences in cost resulted from differences in the machines, though the machines were substantially similar in type.) For only two of the four independents was the factory cost distinctly below the highest factory cost of the International Harvester Company, and for one independent the factory cost was distinctly higher than the cost in any of the four factories of the International Company. In each instance the output of the independent plants was much smaller than the output of any of the International Company's plants, except one. The relative smallness of the independent plants largely explains their higher factory costs. If we prorate over the total factory costs the general and miscellaneous expenses not included in the foregoing figures, the showing of the independent plants is even less favorable. While this may be the result in part of different methods of keeping costs, it is unquestionably due in considerable measure to the comparatively small output of the inde-

[1] Report on the International Harvester Company, p. 260. The basis of the discussion of costs that follows is the above report, pp. 260–265. It should be noted that the raw materials which are produced by the International Company for its own use are charged up to costs on the basis of the prevailing market prices, and, therefore, its costs are comparable with those of the independent producers.

pendent plants. If we add the general and miscellaneous expenses to the factory costs, the average cost of binders for the International Harvester Company during 1910–1911 becomes $58.57, and for the independents $76.18. This difference is considerable, yet, it should be noted, it is no larger than the difference between the costs at the several International plants.

The foregoing differences in costs must not be understood to indicate the relative profit per machine, since the selling expense of the International Company was much higher per machine than that of the independents. Apparently this high selling expense was the result of its elaborate selling organization, which strengthened its hold on the trade and aided it in obtaining a large volume of business. Yet it is still true, in spite of its high selling expense, that the margin of profit for the International Company was larger than it was for the independents.

The International Harvester Company thus found one of its chief sources of power in its lower cost of producing binders,—the most important machine in the harvester trade.

Much the same was true of mowers and rakes. The factory cost of mowers at the four plants of the International Company ranged during the period 1910–1911 from $18.78 to $27.35, and averaged $20.09. For the independents the average was $24.98. For some of the independent plants, therefore, the cost was less than for some of the International Company plants; in fact, at all the independent plants the factory cost was lower than at the plant of the International Company with the highest cost, and at all but two of the independent plants the factory cost was lower than at the plant of the International Company with the second highest cost. While some of the independent plants produced more mowers than did the smallest International plant, yet most of them produced less. None of the independents, however, had an output which could compare with that of the McCormick and the Deering plants, and as a result their costs were higher in comparison. As with binders the selling expense was less for the independent concerns.

The average cost of rakes for the International Company was $10.84, and for the independents $12.47. The factory cost for

the most efficient independent plants was thus much nearer the factory cost for the most efficient of the International Company plants than for either binders or mowers, and therefore the advantage of the trust was less in this branch than in the other two leading branches.

It is clear from what has been said that, generally speaking, the International Harvester Company could produce harvesting machines more cheaply than its competitors.[1] It seems evident, also, that this advantage was mainly due to the large volume of its output. In the harvester business the process of manufacture, which requires the use of a considerable variety of raw materials, is highly elaborate, and large factories with expensive equipment are necessary. Low production costs can be attained only through a minute division of labor; and this involves production on a large scale. It was in the largest plants of the International Company, namely, the McCormick and the Deering plants, that the lowest costs were attained; and in some of the smaller plants the costs were even higher than for the independents. The advantage of the trust in production rested, therefore, to a very large degree on the fact that it included the two largest plants.[2] The important query, therefore, is not whether the trust could produce more cheaply than its smaller rivals (this can hardly be disputed), but whether the McCormick and Deering plants, the largest in the country in 1902 (and because of the volume of their output possessing the lowest costs) became more efficient by virtue of the fact that they entered the trust. To this question no definite answer can be given. One fact, however, is clear. The organization of the International Harvester Company did not reduce the costs of the McCormick and Deer-

[1] For a comparison of the cost of producing harvesting machines in 1916 and in 1918 at the McCormick works of the International Company and at five independent plants, see Report of the Federal Trade Commission on the Causes of High Prices of Farm Implements, p. 669.

[2] The output of binders at the McCormick plant during each year from 1903 to 1911 exceeded by at least eight times the output of binders at any independent plant during the corresponding year. The output of mowers at the McCormick plant was six times greater than the output of any independent.

ing plants through an increase in the volume of their output (perhaps the most important factor leading to low costs), because the volume of production at these plants was as great prior to the merger as at any subsequent date.[1]

Second. Another element of strength was the possession by the International Harvester Company of large financial resources. This enabled it to maintain an elaborate selling organization,—an organization to handle not only harvesting machines, but a great variety of agricultural implements, such as wagons, spreaders, etc., with a consequent saving in the cost of marketing. The possession of large financial resources also made it possible for it to grant long terms of credit to purchasers. The practice of extending credit for considerable periods was originally employed in the harvester business because of the inability of the farmers to pay cash (binders, for example, are quite expensive); and though farmers are now in a better position than formerly to pay cash, the system is still used as a means of getting trade, particularly in foreign countries. The International Company, acquiring a strong financial position by the act of combination, not only retained this practice in the harvesting machine business, but more conspicuously than any other concern extended it to the newer lines, which are generally less expensive, and which were formerly sold on a cash basis. The company was aided in carrying out this policy by the backing of J. P. Morgan and Company, its fiscal agents, and by the loans of Mr. John D. Rockefeller, a father-in-law of one of the McCormicks.

The charge has been made that the International Harvester Company, especially in the years immediately following its organization, resorted to unfair competitive methods. This charge may be briefly considered.

(1) The International Company up to 1905 paraded as independent certain concerns that in reality were not independent. The most important of these concerns was the firm of D. M. Osborne and Company. This practice, however, came to an end in 1905.

[1] Report on the International Harvester Company, pp. 257–258.

(2) The International Company in its commission agency contracts up to 1905 inserted a clause requiring the dealer to handle the company's harvesting machines exclusively.[1] With trust proceedings threatening in several states, this clause was removed in 1905, and was not restored.[2] In fairness to the company it should be said that the exclusive contract clause was customary among harvester companies prior to the establishment of the merger, and that some concerns in the implement trade continued to retain it in their agency contracts even after it was abandoned by the International Company.[3] It might seem as if there were no objection to the requirement that a dealer handle the goods of only one company, since such a provision has the obvious advantage of enlisting the interest of the dealer in the selling of the manufacturer's article. Yet it should be clear that this requirement may result in monopoly. If there are only a few dealers in a given town, and each one of these is given some brand of the trust's harvesters, the requirement of exclusive dealing may shut out the machines of the independent manufacturers, particularly if the machines of the trust are in such insistent demand that a dealer must handle them if he is to do a profitable business.

(3) The International Company so allotted its brands of harvesting machines as to enlist the services of an undue proportion of dealers.[4] Some 95 per cent of the farm machinery in this country was purchased from the local retail dealer; and at most towns there were only two or three dealers.[5] The International Company by giving only one brand of its machines to a particular dealer was able—so the Bureau of Corporations put it—to absorb the services of all or at least a large proportion of the dealers in any one locality. The opinion was common in the trade that the purpose of the company in giving a different line

[1] 81 Kansas Reports 611. According to Brief for the International Harvester Company (no. 56), p. 96, this clause was not enforced.

[2] Report on the International Harvester Company, p. 304.

[3] Brief for the International Harvester Company (no. 757), p. 80.

[4] Report on the International Harvester Company, p. 290.

[5] Ibid., pp. 291, 293.

to each dealer was largely to prevent these dealers from pushing the sales of the goods of competing manufacturers. The representatives of the company denied that they had any such purpose; and urged that even if this was the effect, as claimed by the Bureau of Corporations, it was not an unfair method of competition, if not accompanied by a requirement of exclusive dealing.[1]

(4) Complaint was also made that in some cases the International Company resorted to local price cutting. While there may have been instances of resort to this device, yet in general it was the practice of the company to charge dealers uniform prices for similar machines.[2]

(5) The International Company through its industrial railways obtained excessive divisions of the through rate on the transportation of its goods to market. This was brought to light through an investigation of the Interstate Commerce Commission in 1904.[3] The Illinois Northern Railway and the Chicago, West Pullman and Southern Railway (both controlled by the International Company) operated terminal railroads in the city of Chicago. For the switching services performed by them a reasonable compensation would have been $3.50 and $3.00 per car, respectively. In fact, however, these tap lines received a division of the through rate amounting in some cases to as much as $12 per car. The Commission held that the excess of the amount received by the industrial railways of the International Company over a reasonable payment was in its essence a rebate to the company. This use of the industrial railway to evade the prohibitions of the law forbidding rebates now stands definitely prohibited, and there is no evidence, so far as the author is aware, that the International Company continued to employ the device.[4] Certainly there would be no advantage to the

[1] Brief for the International Harvester Company (no. 56), pp. 101–102.

[2] Report on the International Harvester Company, p. 325.

[3] See 10 I. C. C. Reports 385–404.

[4] According to President Roosevelt (in a letter dated August 22, 1907) the International Harvester Company promised in 1904 to rectify the practices disclosed by the investigation of the Interstate Commerce Commission,

company in its employment after 1913, since in that year the industrial railways were transferred to a separate corporation,—the International Harvester Corporation.

The International Company also made use of price lists, and its salesmen were guilty of misrepresenting the machines of competitors.[1] Yet on the whole the conduct of the company was remarkably free from unfairness in its relations with competitors.[2] Even its competitors testified to this effect. Most, if not all, of its objectionable practices were abandoned some time before the government instituted its dissolution suit; or were the result of competition between agents, and were not countenanced by the higher officials of the company.

The company, furthermore, was not bolstered up by the control of the limited supply of a natural resource (its control over the raw material used to make binder twine,—manilla and sisal fiber,—may possibly be an exception to this general statement); its monopoly position was not due to patent rights (the basic patents had expired prior to its organization); and such tariff protection as it has had has been unimportant.[3] If, therefore, there is such a thing as a "good trust" the International Harvester Company can doubtless qualify as well as any other. The suit brought by the government against this company thus squarely presented to the courts the question as to whether a trust is illegal or not, irrespective of the methods employed by it.[4]

The establishment by the International Company of a monopoly position and the substantial maintenance of that position for a number of years have been shown. What has been the policy of the monopoly with respect to prices?

and it stood ready in 1907 to prove that it had abided by its promise. Cong. Record, April 25, 1912, p. 5318.

[1] Report on the International Harvester Company, pp. 310, 324.

[2] There can be no doubt, said Judge Sanborn of the Circuit Court, "that the consistent and persistent purpose, policy, rule of action, and practice of the defendants has been and is to avoid and prevent all acts and methods unfair, unjust, or oppressive toward their competitors." 214 Fed. Rep. 1008.

[3] Since the passage of the tariff act of 1913 agricultural implements can be imported free of duty.

[4] Cf. p. 436.

The significant comparison, of course, is between prices prior to 1902 and prices after 1902. The only evidence on this point that has come to our attention is a table prepared by the International Harvester Company, showing the price of six foot binders and five foot mowers from 1892 to 1912.[1] From this table it appears that the price of binders advanced in 1900 and 1901 (the two years prior to the organization of the trust), but fell in 1902 (the year the trust was organized) to its former figure, where it remained through 1907. Substantially the same was true of the price of mowers. The government in its Brief conceded that the circular or asking prices of harvesting machines had not materially advanced since 1902, but contended that the prices actually received were not the same.[2] Upon the organization of the trust—so it alleged—the constant shading of prices was stopped, thus leading to an actual increase in the return realized by the International Harvester Company. The defendants counter attacked by pointing out that the government had not called a single witness to testify that prices had been advanced to the injury of the farmer, thus leading to the presumption that no such injury had in fact resulted.[3]

The course of prices from 1903 to 1911 for certain kinds of farm machinery is shown by the table on page 256.

The table shows the average prices realized by the International Company for its chief classes of machines. Slight changes in prices from year to year do not, it should be noted, necessarily indicate any actual change in the prices charged. This is because these prices are generally averages for all types and sizes of a given machine, and a variation in the proportion of machines of the various sizes sold would naturally cause a change in the average price received, even though in the meantime there had been no change in the price of any particular machine. Yet making full allowance for such factors, it is still true that during the period from 1903 to 1911 there was a general advance

[1] See Appendix to Brief for the International Harvester Company (no. 624), p. 286.

[2] Brief for the United States (no. 56), p. 171.

[3] Brief for the International Harvester Company (no. 757), p. 127.

AVERAGE NET PRICES RECEIVED BY THE INTERNATIONAL HARVESTER COMPANY IN THE UNITED STATES FOR SPECIFIED KINDS OF FARM MACHINERY, 1903–1911.[1] (DISCOUNTS, BUT NOT FREIGHT, INCLUDED.)

Machines, etc.	*1903*	*1904*	*1905*	*1906*	*1907*	*1908*	*1909*	*1910*	*1911*
Grain binders, 5, 6, and 7 foot	$98.42 [2]	$97.73 [2]	$97.67 [2]	$95.79	$96.34	$102.65 [7]	$102.49	$102.64	$102.39
Grain binders, 8 foot	....	....	....	109.49	115.63 [3]	122.70 [6]	122.50	122.98	123.74
Mowers [4]	35.11	34.53	34.68	34.48	34.69	37.21 [8]	37.10	37.11	37.06
Rakes [4]	17.30	17.67	17.18	17.11	17.05	18.11	18.18	18.17	18.20
Tedders [4]	29.65	29.12	28.67	28.72	28.22	30.95	30.00	29.74	29.77
Corn binders	96.29	94.25	94.33	93.19	94.89	100.02	99.65	100.19	101.28
Disk harrows [4]	....	....	19.92	19.71	19.91	20.97	20.18	20.25	20.20
Wagons, two horse [4]	....	....	....	....	55.73	58.08	58.66	58.97	58.15
Manure spreaders [4]	....	....	98.74	98.04	96.22	97.39	95.79	89.01	86.29
Cream separators [4]	....	....	70.02	64.37	58.98	51.60	51.35	44.87	44.51
Binder twine, per pound [5]	.1081	.1040	.0972	.1005	.0962	.0822	.0748	.0743	.0647

[1] Report on the International Harvester Company, p. 248.

[2] Includes a number of 8 foot binders.

[3] Price advanced $5.00.

[4] All sizes.

[5] All kinds. Price variations in binder twine were largely due to changes in the price of fiber.

[6] Price advanced $10.00.

[7] Price advanced $7.50.

[8] Price generally advanced $2.50.

in the price of harvesting machines. For example, in 1908 the price of 5, 6, and 7 foot binders was advanced by $7.50; the price of 8 foot binders by $15.00 (1907 and 1908); and the price of mowers by $2.50. Yet to conclude from this statement that the trust made for higher prices would not be fair. Prices of material and of labor were undoubtedly rising, and an increase in prices might therefore have taken place, trust or no trust. Again, the quality of the machines might have improved in the meantime.[1] As bearing on the responsibility of the trust for the advance, we may note that the prices of disk harrows and two-horse wagons, in the manufacture of which competition was quite active, were also advanced in 1908. Again, in 1912 the International Company made a general reduction in the price of its harvesting machines. Grain binders were reduced $5.00, and proportionate reductions were made for other harvesting machines. This reduction was attributed by the company to a decline in the cost of production, yet it is perhaps significant that it was made after the government had begun preparations to file a bill against the company.

Some idea of the reasonableness of the prices charged may be had by an analysis of the profits realized. The profits of the International Company may be determined by two methods: first, by a comparison of its net earnings with its net assets; second, by a comparison of its net earnings with its capital stock and surplus. The table below shows the results by the first method.[2]

RATIO OF NET EARNINGS TO NET ASSETS, EXCLUSIVE OF GOOD WILL, AS COMPUTED BY THE BUREAU, 1903–1911

Year	*Ratio*	*Year*	*Ratio*
1903	0.73[3]	1908	8.73
1904	5.34	1909	13.43
1905	7.01	1910	12.77
1906	6.74	1911	11.51
1907	7.31		

[1] The International Company claims that this was the fact. Brief for the International Harvester Company (no. 56), p. 52.

[2] Report on the International Harvester Company, p. 238.

[3] This is for a period of fifteen months. For an explanation of the low earnings in 1903, see ibid., pp. 207–210.

The average rate of earnings for the nine years was 8.47 per cent; and if we leave out the exceptional year 1903 the average was over 9.00 per cent. A striking fact is the gradual increase in the prosperity of the company. The rate of profit averaged 4.36 per cent during the first three years; 7.59 per cent during the next three years; and 12.57 per cent during the three years following the price advance of 1908. Hence while the profits of the company were quite reasonable on the average, during the later years they were distinctly higher. It should be remembered, however, that in these figures no allowance is made for good will. The company made no entry for good will on its books, and the Bureau found it difficult to compute its amount. Were good will to be included in the net assets, the rate of profit would be much lower.

The second method is to show the profits on the capital stock and surplus.

RATIO OF NET EARNINGS AS REPORTED BY THE INTERNATIONAL HARVESTER COMPANY TO CAPITAL STOCK AND SURPLUS, 1903–1911 [1]

Year	*Ratio*	*Year*	*Ratio*
1903	4.70 [2]	1908	6.73
1904	4.64	1909	10.89
1905	6.08	1910	10.91
1906	5.85	1911	9.95
1907	6.31		

The earnings on the capital stock and surplus averaged 7.34 per cent for the nine years and 10.58 per cent for the last three years. These figures are somewhat below the ratio of earnings to net assets, since the Bureau found the company to be slightly overcapitalized at its organization.[3] Yet had the good will been

[1] Appendix to Brief for the International Harvester Company (no. 624), pp. 163–164.

[2] Computed on the capital stock ($120,000,000).

[3] Through the reinvestment of surplus earnings the original deficiency in physical assets had been entirely overcome by the end of 1908, and up to the stock dividend of 1910, at any rate, the company was undercapitalized rather than overcapitalized. Report on the International Harvester Company, p. 25.

included in making the earlier calculation, the result might have been different.

It is apparent that by either method of calculation the earnings of the International Company were moderate.[1] And even more moderate were the dividends actually disbursed to stockholders. The rate of dividend was 3 per cent in 1903, and 4 per cent in 1904, 1905, and 1906. In the latter year the stock was divided into $60,000,000 preferred and $60,000,000 common. On the preferred a rate of 7 per cent was begun in June, 1907, and this rate was regularly paid thereafter. No dividend was paid on the common stock during 1907–1909. In 1910 a 33 1/3 per cent common stock dividend was declared, and a quarterly dividend of 1 per cent inaugurated. In 1911 the rate was increased to 1 1/4 per cent quarterly.

It is worth noting, in closing this subject, that the rate of profit obtained by the International Company was much greater for its highly monopolized lines—that is, harvesting machines—than for the newer lines, such as wagons and spreaders.[2] In other words, the influence of monopoly on prices and profits is somewhat obscured by the fact that the figures given are for the total profits of the International Company rather than for its profits in those branches that were monopolized.

[1] Some tables showing the earnings of the International Company from 1913–1918 may be found in the Report of the Federal Trade Commission on the Causes of High Prices of Farm Implements, pp. 90–95.

[2] Report on the International Harvester Company, p. 240.

CHAPTER XI

THE EFFECT OF TRUSTS ON PRICES

Having surveyed the trust movement and having studied in detail a number of representative trusts, we may now turn to an examination of the underlying causes of the trust movement. An understanding of the reasons for forming trusts will enable the reader more readily to comprehend the popular attitude toward them as evidenced in legislative enactments and judicial proceedings; and will greatly assist him in determining what the public policy with respect to them should be.

The primary explanation of the trust movement, notably that characterizing the period from 1898 to 1903, would appear to be the desire of the manufacturers to restrict or eliminate competition, and thus to establish monopoly prices. Whether this competition that it was desired to eliminate was "ruinous" in its nature is a question we have analyzed elsewhere at considerable length, the conclusion being that competition can not properly be regarded as ruinous, except possibly in a quite limited range of industries.[1] A secondary influence was the hope of achieving the economies of the trust form of organization,—a topic that will receive consideration in chapter XIX. Third, though of less importance, was the lure of large profits for the trust promoters, men who conceived the idea of a trust in a given industry, or, if they did not conceive it, at least carried it through to a successful consummation. There were other incentives, to be sure, such as the ambition of certain individuals to become Napoleons of industry, but undoubtedly these were the three principal motives. First, then, as to the trust and prices.

The evidence as to the effect of trusts on prices has been presented for a number of trusts; and may be briefly summarized at this point. In making this summary and throughout the sub-

[1] Quarterly Journal of Economics, 34, pp. 473–519 (1920).

sequent discussion the endeavor will be made of course to avoid a dogmatic presentation; the difficulty of speaking with positiveness on this perplexing matter is fully realized. It is easy to show that on innumerable occasions the organization of a trust or the tightening of monopoly control has been accompanied by higher prices, yet one can not always be certain that prices would not also have advanced under competitive conditions. Despite the difficulties, however, it is believed that both history and general reasoning establish the tendency of the trusts to increase prices. First, as to the teachings of experience.

One of the earliest and most powerful trusts was the Standard Oil Company. The prices charged for oil by this company formed the subject of an unusually elaborate study by the Bureau of Corporations, as the result of which the Bureau was able to speak with confidence and authority concerning the effect of the oil trust on prices. The Standard Oil Company, so the Bureau noted, had repeatedly claimed that it had reduced the price of oil; that it had been a benefit to the consumer; and that only a great combination like the Standard could have furnished oil at the prices that had prevailed. "Each one of these claims," said the Bureau, "is disproved by this report." With regard to the period to 1897, though the price statistics for these early years were by no means complete, yet making all the necessary allowances "they demonstrate the falsity of the historic claim of the Standard Oil Company that by reason of its extraordinary efficiency it has brought prices to a point lower than would have been reached had business remained under normal competitive conditions and in the hands of a number of comparatively smaller concerns." [1] For the period following 1897 and down to 1905 the statistics were very full, having been collected by the Bureau directly from thousands of retail dealers throughout the country. A careful analysis of these figures establishes, said the Bureau, that "the Standard had consistently used its power to raise the price of oil during the last ten years, not only absolutely but also relatively to the cost of crude oil." [2] The Bureau as-

[1] Report on the Petroleum Industry, part II, p. XXXIII.
[2] Ibid., p. XXX.

serted that the Standard had used its monopolistic power to "oppress the public through highly extortionate prices," and the truth of this assertion is abundantly demonstrated by the voluminous evidence presented in its report on oil prices.

The effect of trusts on prices is shown in illuminating fashion by the experience of the sugar trust. The story is found on pages 116–119. Briefly summarized, it appears that the margin between the price of raw sugar and of refined sugar was high during the early eighties, and declined rapidly after 1882 and until 1887 (the year in which the sugar "trust" was formed). The decline in the margin between 1882 and 1887 reflected the keen competition that prevailed,—a competition so severe that only those refiners who realized the economies of large-scale production were able to operate at a profit. Many refiners, particularly those who failed to envisage the inevitable trend toward larger production units, were indeed obliged to withdraw permanently from the business. In October, 1887, the "trust agreement" became effective; and the margin rose from three-quarters of a cent per pound (in 1887) to one and one-quarter cents (in 1888), an increase of approximately 65 per cent. No doubt the margin was abnormally low prior to the formation of the "trust"; and therefore it is difficult to say how much of the increase is fairly attributable to it. The high margin of 1888, however, speedily attracted new competition; and as a result the margin fell in 1890 to an even lower figure than during the eighties. In 1892 the trust, through the acquisition of a number of competitors, secured nearly a complete monopoly of the sugar refining industry; and the margin was considerably advanced once more. As before, this induced new competition, as the result of which the margin fell below the cost of refining. Upon the acquisition of several competitors in 1900, prices and margins again went up; but this led to the construction of competing refineries, and in 1904 the margin again declined. Taking therefore the first eighteen years of the life of the trust—the margin after 1905 indicates the existence of competitive conditions—it appears that sugar prices were low when competition was present, and were advanced when competition was absent or

brought under control. The conclusion seems to be justified that the trust made for high prices, and that it did little, if anything, to steady them.[1]

Trusts in the steel industry seem also to have made for higher prices of steel products.[2] The most important of the trusts organized in the various branches of the iron and steel industry during 1898 to 1900 were the American Tin Plate Company, the American Steel and Wire Company, and the National Tube Company—the Carnegie Company, the Federal Steel Company, and the National Steel Company were mammoth combinations, the first two doing a larger business in the aggregate than any of the steel trusts, yet they did not individually monopolize any important branch of the trade. The American Tin Plate Company was organized in December, 1898, for the purpose, according to its president, "of getting together to do away with foolishness in making prices."[3] For several years prior to its formation the price of tin plates had shown a declining tendency, the average monthly price at New York per hundred pounds being $3.50 in January, 1896 (the maximum for 1896–1898), and $2.89 in December, 1898.[4] From that month on it steadily increased until by September of the following year it had reached a monthly average of $4.83, or nearly $2.00 per hundred pounds higher than when the trust was formed. The price remained at this figure without deviation of more than a cent until August, 1900. By October of 1900 the price had fallen to $4.19, where it remained unchanged for two years.[5]

The American Steel and Wire Company of New Jersey was organized in January, 1899. During the preceding year the price of wire nails at Pittsburg had averaged $1.34 per hundred pound keg, being $1.29 in December, 1898.[6] The price advanced

[1] On this latter point see Jenks and Clark, The Trust Problem, pp. 138–139.

[2] See pp. 196–197, 203, 225–230.

[3] Industrial Commission, I, p. 885.

[4] Brief for the United States (no. 481), vol. II, p. 1047.

[5] See Jenks, Bulletin of the Department of Labor, vol. V, no. 29, p. 735, for a table showing that the increase in the price of tin plate during 1899 was much greater than the increase in the cost of raw materials.

[6] Brief for the United States (no. 481), vol. II, p. 1045.

steadily throughout 1899, the average for the year being $2.32 per keg, or nearly 75 per cent higher.[1] By January, 1900, the price had reached $3.20 per keg, but it did not long remain at this height. The outbreak of competition during the middle of 1900 brought the price down to $2.20 per keg, yet this was much above the price that had prevailed prior to the formation of the trust, and more than the trust was able to get in the years that followed. The price of plain wire at Pittsburg followed the same general movement. From a figure of $1.13 per hundred pounds in December, 1898, it rose to $3.05 in January, 1900, and then declined to $2.15 in May. During the same period the price of barbed wire advanced from $1.75 per hundred pounds to $3.80 per hundred pounds.[2] Mr. Gates, the chairman of the company, testified in November, 1899, that the rapid advance in the price of barbed wire was no doubt due to the fact that the company had a complete monopoly.[3]

The National Tube Company was organized in June, 1899. The year previous to its formation the price of tubes was $30.00 per gross ton; the year of its formation, $67.00 per ton; and early in the year after its formation, as high as $89.00 per ton.[4]

But it is not at all clear to what degree the trusts were responsible for these increases in prices. These early steel trusts were formed during a period of prosperity, which would have led to higher prices even in the entire absence of artificial inflation. Costs, moreover, were advancing, since the prices of raw materials likewise responded to the heavy demand. The prices of the finished products, however, increased more rapidly than costs, and as a result profits were unusually large. Whether prices and thus profits were higher than they would have been had it not been for the trusts is a question that can not be answered with certainty. However, such would appear to have been the case;

[1] The advance in prices was greater than the increase in raw material costs. See Jenks, Bulletin of the Department of Labor, vol. V, no. 29, p. 744.

[2] Brief for the United States (no. 481), vol. II, p. 161.

[3] Industrial Commission, I, p. 1009.

[4] See p. 196.

and certainly the trust organizers in enormously overcapitalizing the properties anticipated such an outcome.

As is indicated by the table on page 203, the formation of the United States Steel Corporation was not followed by as considerable an advance in the prices of steel products as was the case on the formation of the earlier steel trusts. The prices in May, 1901 (the first month after the organization of the Corporation) were higher than the prices in October, 1900 (the last month in which competition was active) for every product shown except tin plates, yet the increase was not so noteworthy as in the case of the earlier trusts. No doubt a partial explanation is the fact that the combination and trust movement in this industry during 1898 to 1900 had already established prices on a high level. It would appear also that the managers of the Corporation, profiting by the experience of the earlier trusts, had chosen to charge more moderate prices in order to discourage potential competitors. The real influence of the organization of the Steel Corporation would be best shown, of course, by a comparison of the prices that prevailed in 1901 with those that would have prevailed in 1901 (and subsequent years) had the battle of giants been allowed to proceed; but this comparison obviously cannot be made.

The extent of the control exercised over prices by the Steel Corporation is well shown by the movement (or lack of movement) of steel rail prices. This matter is discussed on page 229. The Corporation's practice of maintaining the same prices over comparatively long periods was employed also in the case of billets, plates, structural steel, tin plates, wire, wire nails, bars, and black sheets, though by no means to the same degree.[1] The policy was possible, however, only because of coöperation with its competitors as arranged through the so-called Gary dinners and other devices. That these prices were highly profitable is proven by the enormous profits obtained by the Corporation, enabling it within fifteen years more or less to squeeze out the water from its stock, which at the beginning had little behind it but the hope of monopoly gains.

[1] See Brief for the United States (no. 481), vol. II, pp. 1038–1047.

The tobacco trust was fully investigated by the Bureau of Corporations, and a volume dealing particularly with prices, costs, and profits was issued. Nevertheless for several reasons it is difficult to speak positively concerning the effect of the trust on prices. Thus, the American Tobacco Company when organized in 1890 secured control of the cigarette business, yet detailed data covering prices of cigarettes are not available for the years prior to 1893. After 1893 the net price of cigarettes less taxes steadily declined until 1899, and then rapidly advanced almost uniformly down to 1910.[1] However, these price movements were roughly in harmony with costs; the profit per thousand remained fairly steady throughout the whole period. That the prices were highly remunerative is shown by the analysis of profits on pages 161 seq.

The proportion of the little cigar business done by the trust is not known for the years prior to 1898. In that year it produced less than 50 per cent of the little cigar output of the country. Its share of the business steadily increased until by 1910 it amounted to over 90 per cent of the total. Likewise the profit per thousand steadily increased, being 41 cents per thousand in 1898, and $1.03 per thousand in 1910.[2] Net prices (less tax) were no higher in 1910 than in 1898, but costs were very much lower. The trust thus kept for itself all the benefits of declining costs.

For plug tobacco the statistics are more complete.[3] In 1894 the net price of plug tobacco less taxes amounted to 29.1 cents per pound. At that time no one company dominated the industry. During 1894 the American Tobacco Company instituted a campaign for the domination of the plug business, and prices were severely cut, falling to 12.2 cents per pound in 1897. Early in 1898 a combination was agreed upon, and the price for the year rose to 16.7 cents per pound. During the following year the Liggett and Myers Tobacco Company was

[1] See p. 155.

[2] Report of the Commissioner of Corporations on the Tobacco Industry, part III, p. 182.

[3] See pp. 157–159.

acquired, and the price averaged 21.0 cents, and in 1900, 22.8 cents. In the years that followed control was made effective, and prices and profits increased. By 1908 (the high-water mark for prices down to 1910) the price had reached 30.3 cents, and the profit 8.0 cents, as compared with a loss during each year from 1895 to 1898. The appropriation by the trust of the benefits of the remission of the Spanish-American war taxes also testifies to the power and workings of trusts.

Similar results appear upon an examination of the prices and profits obtained in the smoking tobacco and snuff branches. A comparison of the latter business (the most highly monopolized branch of the tobacco industry) with the cigar business (the least monopolized branch) is unusually instructive in its bearing on the comparative results of monopoly and competition. On this point the reader is referred to page 159.

The data are not available to determine what influence has been exerted on prices by the harvester and shoe machinery trusts, the two remaining trusts of those described in some detail. So far as the harvester trust is concerned,[1] it does not appear that it has increased prices to an appreciable degree. The Department of Justice made the allegation that while the circular prices of harvesting machines were not increased upon the organization of the trust in 1902, the prices actually received did increase through the abandonment of price cutting. However, the government introduced no evidence to support this allegation, and the company unequivocally denied it. The Bureau of Corporations in its report on the International Harvester Company devoted comparatively little space to the subject of prices, but concluded that the company had taken advantage of its monopolistic position in harvesters to increase both prices and margins, while reducing prices in those outside lines in which it had to meet keen competition.[2] It is easy to show, of course, that there was a general advance in the price of harvesters during 1903 to 1911, yet this was a period of rising prices and costs, and hence it would not be fair in the absence of complete information

[1] See pp. 254–257.

[2] Report on the International Harvester Company, p. 255.

to attribute the advance to the trust, particularly since the price of some agricultural implements that were subject to competition likewise advanced. The fact is that the International Harvester Company during the period from 1903 to 1911 earned a comparatively moderate return on a capitalization singularly free from water. In part, of course, this low rate of return resulted from the fact that its profits on the competitive lines were combined with its profits on the monopolized lines, thus tending to obscure the influence of monopoly on prices and profits.

The whisky trust is not one of the concerns described in detail in the preceding chapters. However, the prices charged by it have been carefully investigated by Professor Jenks;[1] and we may summarize his conclusions. Professor Jenks points out that immediately after the organization of the whisky "trust" in 1887 the prices of spirits were reduced rather than advanced. However, this reduction in prices was designed to force the remaining competitors into the "trust"; and when this purpose had been accomplished prices were increased, and the profits became very large. The profits were so good in fact that new distilleries were constructed, and accordingly in 1889 prices had to be cut to crush the new competition. In 1890 the "trust" reorganized under the corporate form; and during the middle of 1891 acquired its principal rival. Prices and margins thereupon increased. Early in 1893 the price and the margin were at a very high point, but by the middle of 1894, because of competition, speculation, and poor management on the part of the trust officials, the price had fallen very low, and the margin had entirely disappeared. In January, 1895, the trust went into the hands of a receiver.

We need not follow the whisky trust through its checkered career. It will suffice to state Professor Jenks' conclusion that the trust was able to control the price of spirits rather effectively for comparatively short periods after each reorganization; and that at times it used this control to increase prices and margins, and at other times it reduced prices to injure its competitors. On

[1] See The Trust Problem (1917), pp. 141–149; Bulletin of the Department of Labor, vol. V, pp. 726–731; Political Science Quarterly, 4, pp. 309–314, and 5, pp. 495–497.

the whole, however, either because of the persistence of competition or because of the policy of the management, prices, down to 1898 at least, were less stable than prior to the formation of the trust.[1] In the later years of its life, notably after 1900, the trust adopted the policy of charging more moderate prices in the hope of keeping competition within bounds.[2] Like many other trusts it had found that a grasping policy defeated its own ends by artificially stimulating production, and thus making impossible the maintenance of prices at a profitable level.

That the trust organizers anticipated that the establishment of monopoly conditions would permit the charging of prices above a competitive level is indicated by the huge structure of overcapitalization that they erected.[3] Generally speaking, the capitalization of the trusts was twice as large as the value under competitive conditions of the properties and businesses that they acquired. Usually the preferred stock represented the value of the plants prior to their union in the trust, and the common stock the hope of monopoly profits. Returns on the common stock of the trust, unbacked as it was by property, might be reaped were one of two results achieved: first, a reduction of costs consequent upon the realization of the economies of the trust form of organization; or second, the elevation of prices to a monopolistic level. No doubt the trust organizers intended to take full advantage of both of these opportunities in the endeavor to earn satisfactory dividends on the common stock as well as on the preferred stock, yet if the conclusions of chapter XIX are sound, their best prospect of success was through the raising of prices.

That the common stock of most of the trusts was "water," that is, had no actual property behind it, is nowhere seriously questioned. The following well authenticated facts bearing on

[1] Bulletin of the Department of Labor, vol. V, p. 731.

[2] Industrial Commission, I, p. 814.

[3] The term overcapitalization as here employed refers to a capitalization in excess of both the investment and the reproduction cost. A successful trust might be able to earn normal returns on "watered" stock, yet this indicates not so much the reasonableness of the capitalization as the enjoyment of monopoly profits.

some leading trusts would appear to "make assurance doubly sure."

The value of the property acquired by the Steel Corporation in 1901 was the subject of a painstaking study by the Bureau of Corporations.[1] In this investigation three different bases were used,—the investment of the constituent companies at the time of their formation, the average market value of their securities from the date of their organization to the close of 1900, and the value of the properties as evidenced by a physical valuation. The conclusion of the Bureau was that the common stock of the Corporation, amounting to 36 per cent of its total capitalization, was water; and that from one-fifth to two-fifths of the preferred stock, this stock also amounting in the aggregate to 36 per cent of the total capitalization, was water, the amount of the over-capitalization depending on the basis of valuation employed. By either the investment or the physical valuation basis, slightly over 50 per cent of the total capitalization had no assets behind it; and by the market value of the securities basis, reflecting, as it did, the monopoly profits of the constituent companies, the percentage was 43. This tremendous overcapitalization, proven in the case of the Steel Corporation, was characteristic also of the earlier steel trusts, as is established in the report of the Bureau of Corporations.[2] This was admitted also by Judge W. H. Moore, a well-known trust promoter, when in testimony before the Industrial Commission he said: "everybody knows what they are getting when they get common stock; they know they are not getting anything that represents assets." [3]

The various tobacco trusts were also heavily overcapitalized. The cigarette trust (the original American Tobacco Company) was capitalized at $25,000,000. The Bureau of Corporations

[1] See pp. 208–210.

[2] See Report on the Steel Industry, part I, pp. 127–133 (American Steel and Wire Company); pp. 133–136 (American Tin Plate Company); pp. 138–139 (American Steel Hoop Company); pp. 139–141 (American Sheet Steel Company); pp. 141–144 (National Tube Company); and pp. 144–145 (Shelby Steel Tube Company). See also Brief for the United States (no. 481), vol. I, pp. 22, 26, 29, 31, 33.

[3] Industrial Commission, I, p. 963.

found that the tangible assets of the constituent companies amounted to $5,370,462 (including $1,825,354 in notes of the organizers),[1] and the good will to $8,954,892; or an overcapitalization exceeding $10,000,000.[2] The Continental Tobacco Company (the plug tobacco trust), after acquiring the Liggett and Myers Tobacco Company in 1899, had a capitalization of $97,690,700, one-half preferred stock and one-half common. The company entered $26,831,123 of this on its books as tangible assets, and the balance ($70,859,577) as intangible assets. The Bureau declared that the value of the intangible assets, measured on a cash basis, was not over $16,664,867; and the overcapitalization therefore amounted to $54,194,710.[3] Over 55 per cent of the company's securities might therefore be regarded as water. The American Snuff Company (the snuff trust) was also heavily overcapitalized. At its organization in 1900 it was capitalized at $23,001,700, of which $12,000,000 was preferred stock and $11,001,700 common. The Bureau found that the tangible assets of the constituent concerns were worth $4,312,728, and the good will not over $7,689,000, or a total of not to exceed $12,001,728. All of the common stock, therefore, was water.[4]

Despite their excessive capitalization these trusts all paid large dividends on their stock, water and all. Their ability to do so testified, as said before, not to the reasonableness of the capitalization, but to the possession of monopoly earnings. In contrast, the American Cigar Company, which hoped to monopolize the cigar industry, earned only a moderate return on a capitalization free from water, yet this was because it did not succeed in effecting a monopoly of its branch of the business, and it was therefore unable to raise prices above a competitive level.

Among the other trusts that were overcapitalized, some of

[1] Against these notes an entry was immediately made on the books of the company to surplus, so that the capital and surplus amounted to $26,825,354.

[2] See p. 123.

[3] Report on the Tobacco Industry, part II, pp. 12, 99.

[4] Ibid., pp. 28–29.

them quite heavily, were the following: the American Sugar Refining Company,[1] the American Can Company,[2] the Distilling and Cattle Feeding Company and its successors,[3] the National Starch Manufacturing Company (the starch trust),[4] the Glucose Sugar Refining Company (the glucose trust),[5] the Corn Products Company (the starch and glucose trust),[6] the Corn Products Refining Company (the successor to the Corn Products Company),[7] the International Paper Company,[8] the American Bicycle Company,[9] the American Malting Company,[10] the Asphalt Company of America,[11] the Mount Vernon-Woodberry Cotton Duck Company,[12] the National Cordage Company,[13] the National Salt Company,[14] the National Shear Company,[15] the New England Cotton Yarn Company,[16] the Rubber Goods Manufacturing Company,[17] the United States Leather Company,[18] and the United States Rubber Company.[19]

Some trusts, on the other hand, have been capitalized on a moderate basis. Among them the most conspicuous illustrations

[1] Industrial Commission, I, p. 13 (Review of Evidence). See also pp. 120–121.

[2] 230 Fed. Rep. 870–871, 877.

[3] Industrial Commission, I, p. 14 (Review of Evidence).

[4] Ibid., XIII, p. 673.

[5] Brief for the United States in United States *v.* Corn Products Refining Company (no. E-10–122), p. 485; and Dewing, Corporate Promotions and Reorganizations, pp. 79, 532.

[6] Dewing, op. cit., pp. 89, 93–95.

[7] Ibid., pp. 106, 108–109.

[8] Industrial Commission, I, pp. 409–410, 415–416, 419–420, 432–433, 441.

[9] Dewing, op. cit., pp. 254, 532.

[10] Ibid., pp. 278–279, 296, 532.

[11] Ibid., pp. 432–433, 532.

[12] Ibid., pp. 342–343, 532.

[13] Industrial Commission, XIII, p. 130; Dewing, op. cit., pp. 123, 532.

[14] Industrial Commission, XIII, pp. 249–250; Dewing, op. cit., pp. 207–208, 532.

[15] Industrial Commission, I, p. 1044.

[16] Dewing, op. cit., pp. 313–316, 325, 532.

[17] Industrial Commission, XIII, pp. 37, 47.

[18] Dewing, op. cit., pp. 20, 23, 532.

[19] Industrial Commission, XIII, p. 48.

are the Standard Oil Company,[1] the International Harvester Company,[2] the Pittsburg Plate Glass Company,[3] and the meat-packing companies.[4]

The ability of the trusts to charge excessive prices and to capitalize the increased earning power thus created must be ascribed in many cases to the protection afforded by the tariff. Had it not been for the prohibitions, partial or complete, imposed by the tariff, foreign competition would have operated to prevent prices in this country from being raised above the foreign cost plus transportation expenses. And if prices could not be much advanced as the result of the elimination of domestic competition, there would have been no justification, even on the earning power basis, for the issuance of a mass of watered securities, unless indeed the trust should prove to be much more efficient than the producing units that it displaced.[5] The protective tariff thus promoted the trust movement by offering to the manufacturers prospects of large profits—profits large enough to induce them to overcome their inherent repugnance to relinquishing their independence and the control of their own business—and by offering to the investing public a chance to share in the speculative gains.[6]

However, the influence of the tariff must not be exaggerated. Trusts were formed in industries not protected by tariff duties as well as in industries enjoying such artificial support; and they were formed in industries in which such protection was purely nominal as well as in industries in which the trusts required

[1] If we compare the capitalization of the Standard with the actual investment (exclusive of the reinvestment of surplus earnings) it was overcapitalized in 1906; if we compare it with the cost of reproducing the property on that date it was distinctly undercapitalized. See Brief for the United States (no. 725), vol. II, pp. 4–5.

[2] See p. 236.

[3] Industrial Commission, XIII, pp. 227, 241.

[4] Report of the Commissioner of Corporations on the Beef Industry, pp. 39–40.

[5] This matter is discussed in ch. 19.

[6] The tariff also furthered the trust movement by intensifying competition in the protected industries. On this point see Bullock, Quarterly Journal of Economics, 15, pp. 208–209.

assistance were they to compete successfully with foreign manufacturers. Clearly the tariff can not be held responsible for the formation of trusts in those industries in which the efficiency of American manufacturers was so pronounced that domestic prices remained lower than foreign even after the elimination of competition in this country. The truth is that the causes of the growth of monopoly are numerous and complex, and the most that can be said with respect to the tariff is that in many instances it was a contributing factor of considerable importance.

So much for conclusions grounded on experience. Let us next consider on the basis of general reasoning what is the probable effect of monopoly on prices.

According to the theory of monopoly price, a monopolized article will be sold at the price that yields the maximum net profits.[1] If a high price be charged, the profit per unit will be large, but the volume of sales will be small, unless the demand be inelastic. If, on the other hand, a low price be charged, the profit per unit will be small, but the volume of sales will be large, providing the demand is elastic. Under these circumstances the monopolist (trust) may be expected in the absence of restraining factors—of which more later—to hit upon, through a process of trial and error, that price which brings in the greatest net revenue. What that price will be will depend, as stated before, on the conditions of demand. In general, a high price will be more profitable if the demand is inelastic, that is, if it persists despite high prices; and a low price will be more profitable if the demand is elastic, that is, if it increases as the price falls, and decreases as the price rises. What will be the most profitable price will depend also on the conditions of cost. If the cost of production rises as the volume of output increases, the tendency will be to pursue a high price policy, since increased business occasions a greater expense per unit. This will be particularly true, if at the same time the demand is inelastic. If, however, the cost of pro-

[1] For a more extended discussion of the theory of monopoly price, see Taussig, Principles of Economics (1911), I, ch. 15; Ely, Outlines of Economics (1916), pp. 200–207; and Ely, Monopolies and Trusts, ch. 3.

duction falls as the volume of output increases, the tendency will be to pursue a low price policy, since enlarged business causes a reduced expense per unit. If the demand be elastic, the monopolist will be almost certain to charge comparatively low prices. If, finally, the cost be neither increasing nor decreasing, but constant, the calculations of the monopolist will be more simple; he will adjust his output with reference solely to the demand, choosing that price that promises the maximum net returns.

Such being the principles underlying the determination of monopoly price, how does a monopoly price compare with a competitive price? There is general agreement among leading economists that a monopoly price is likely to be higher than a competitive price.[1] The explanation of this tendency lies in the control exercised by the monopoly over the supply. Under competitive conditions the price of an article tends to hover about the cost of production (including in cost a normal profit). If the price rises above the cost, the supply increases and the price falls again, provided there has been no change meanwhile in the conditions of demand; and if the price falls below the cost, the supply decreases and the price rises again. Under monopoly conditions, however, the price of an article does not tend to hover about the cost of production, but at a point somewhat above; for the monopolist can limit the supply, and by this means prevent prices from falling to a level determined by cost. To be sure, the monopoly in restricting the supply and advancing the price is confronted with the possibility of a considerable decline in its sales; and it may find it advantageous to pursue a moderate policy. But the competitive producer charging a high price will not only suffer a reduction in his sales through the decline in the demand, but also through a diversion of his business to his

[1] Taussig, Principles of Economics (1911), I, p. 206; Ely, Monopolies and Trusts (1906), p. 119; Fisher, Elementary Principles of Economics (1912), p. 330; Carver, Principles of Political Economy (1919), p. 352; Bullock, Introduction to the Study of Economics (1908), p. 337; Fetter, The Principles of Economics (1910), p. 330; Seligman, Principles of Economics (1910), p. 258; Seager, Introduction to Economics (1905), p. 498.

competitors. To a monopoly, assuming it to be effective and to have competition well under control, there is one check on high prices, whereas to a competitive producer there are two. It is of course evident that an individual competitive producer can restrict his own supply, and thus raise prices somewhat, yet he can not ordinarily by such means enhance his *profits*. The benefits of the high price go to his fellow producers who continue production in undiminished volume; and are temporary at best, since the high prices stimulate the output. To the consuming public this is precisely the merit of the competitive system, that under it a particular producer can not augment his profits by restricting the output. A monopoly, on the other hand, may achieve its success, not by increasing, but by limiting production.

The monopoly price, it should be observed, may be no higher, and may even be lower, than the competitive price, if the monopoly is more efficient than alternative forms of business organization. The monopoly under these conditions would still charge the price that was the most profitable to it, but this price might be below the cost of production (including a normal profit) to smaller concerns. Whether this is to be anticipated so far as industrial monopolies (trusts) are concerned will receive consideration later.[1]

If these are the principles upon which monopolies proceed, how does it happen that it is difficult to show in convincing fashion the whole effect of trusts on prices? The explanation is that there are many considerations that have made it seem advisable for the trusts to exercise restraint in their price policy, with the result that they have not advanced prices as much as might be anticipated did they feel entirely secure in their monopolistic position.

(1) First of all there is the potential competition of new concerns. If the trust is too greedy for profits and raises prices unreasonably, there are attracted to the industry a host of new companies anxious to participate in the unusual returns. During the early life of the trust movement the individual trusts

[1] See ch. 19.

frequently tried to do away with this competition by the resort to unfair competitive tactics, notably local price cutting, railroad discriminations, and exclusive dealing requirements; and endeavored through threats of employing such practices against all would-be competitors to prevent new concerns from ever getting started. Such methods resulted in the destruction of many enterprises, and may be said to have been reasonably successful in many instances. Yet they were not always used, and even when used they were by no means always effective. In many industries the trusts found themselves overcome by the new competition, and their control of the trade speedily dwindled away. The lesson was salutary, and the trusts that survived pursued a more farsighted policy. They commonly came to see the inadvisability of charging prices so high that new concerns were tempted to rush headlong into the business hoping to get their capital back in a few years, for such a policy led to serious overproduction and to an inevitable decline in prices. They charged instead more moderate prices, albeit somewhat above a competitive figure. It thus appears that potential (and actual) competition has operated on occasion to prevent the trusts from following their natural course. Yet potential competition is not a satisfactory or adequate regulator of trust profits, because the strength of many trusts is based on the possession of some special advantage in competition, such as the ownership of patents or a limited natural resource. When this is the case, there are effective obstacles, perhaps insuperable ones, in the way of competition, and the trust need exercise little restraint, unless there be danger of hostile legislation of one kind or another. Again, in some industries, though competition is not artificially restrained, it may be backward because of the large capital needed to embark in the undertaking, or because of the length of time required to construct the plant and to establish the business. In such industries the possibility of reduced prices on the emergence of competition may prevent potential competition from becoming actual competition, and may enable the trust to charge prices that are considerably above the cost of production, and thus to secure a monopoly profit.

(2) The possibility of substituting for the monopolized article another one that is being sold at a more reasonable price is a factor that may induce trusts to refrain from charging exorbitant prices. If the price of kerosene be abnormally high, people will use gas and electricity; and no doubt the competition of these fuels has operated to keep down the price of kerosene, and thus outwardly to lend support to the argument that the oil trust has reduced its price. If the price of sugar be excessive, erstwhile consumers will adopt such substitutes as glucose. In industry, manufacturers may employ as fuel soft coal, hard coal (the steam sizes), gas, oil, and the like; and they may even burn no fuel, but run their machinery with electricity generated by water power hundreds of miles away. In homes, wood is also a possible substitute. Steel, lumber, concrete, stone, and brick all compete with one another to some extent in building. Rubber shoes (or soles) may be substituted for leather shoes; and enameled ware and tin may be used in place of aluminum cooking utensils. Even the tin can trust must bear in mind that an excessive price for tin cans may hamper the fruit preserving industry in its competition with the fruit drying industry. However, the possibility of substitution is not always present, or, if present, may exercise comparatively little influence. What, it may be asked, are effective substitutes for watches, cameras, cigarettes, salt, grain binders, and steel rails? Moreover, when the competition of substitutes is effective, there is an incentive to secure control over the allied industry, which explains the entrance of Standard Oil capitalists into the gas industry, and the attempted domination of the substitutes for meat by the leading meat-packers. The conclusion would appear to be justified that while collateral competition may impose some limitations on monopoly power, it by no means insures that the monopolized article will be sold at a reasonable price, and it is thus a safeguard of limited effectiveness.

(3) A particular trust may be restrained by the fact that its sales are made in large part to another trust, or possibly to an important combination. For example, a copper trust, if obliged to sell to a brass trust, might meet with determined resistance to

exorbitant prices; the latter by withholding purchases might well break the market. A tin can trust in such fashion might secure relief on its purchases of tin plate. However, it rarely happens that one trust is the principal market for another. The shoe machinery trust and the cash register trust buy large quantities of steel, yet their purchases constitute such a small percentage of the total that such action as they individually might take to reduce the price charged for steel by a steel trust would be of little consequence. So it would be with the purchase of cotton yarn by the thread trust, and of steel pipes and tubes by the oil trust. It is precisely because of their limited control over the affairs of other trusts that some of them make for themselves the articles which they would otherwise have to secure from their fellow trusts. This explains in large measure why the oil trust, the tobacco trust, and many others make their own tin cans instead of buying them from the American Can Company. We must conclude that the balance of power among trusts, though it protects the consumer in part, is not an effective bar against excessive prices of trust made goods.

(4) The disinclination to arouse public opinion also plays its part, and no doubt a considerable one. The people, if sufficiently antagonized, will repeal favoring legislation or pass restrictive laws. Many trusts have been protected against foreign competition by protective duties; but the trust that uses these duties as an excuse for unreasonable prices faces the danger of a removal of its protection. Other trusts are founded on patent monopolies permitted by the government; but the patent laws can be revised, if it seems desirable. But not only may favoring legislation be repealed, but regulative laws may be passed. At the present time (1919) bills to regulate the meat industry are receiving the serious consideration of Congress; and the suggestion at one time or another has been soberly made that the oil and the steel industries (and others) are essentially public service corporations, and should be regulated as such. Indeed, a considerable body of public opinion favors the regulation of the prices of all monopolized articles. Another considerable group advocates public ownership of natural resources, a step that would be of

particular concern to some ten important trusts. In view of these contingencies it is likely that the trust managers, with their fingers on the public pulse and with an eye to the continued enjoyment of their strategic position, will refrain from pressing their advantage to the fullest; and their prices will not in the future, as they have not in the past, conform rigidly to the principles of monopoly price as above laid down.

(5) A trust, it has been said, may be influenced by a sense of equity and reasonableness; it may desire to have the good will of the dealers and the public, and thus may not take advantage of their necessities. The steel trust, for example, fixed the price of steel rails at $28 per ton, and charged no more than this during periods of prosperity, when market conditions would have enabled it to get more. In this particular instance the price was fixed at a very high level to begin with, hence this is hardly an illustration of equitable dealing. Yet it is conceivable that a trust, even though created in an anti-social spirit, might come under the leadership of managers of a different sort,—managers desirous of charging only a fair price. Conceivable though it be, it is unlikely, since even under the competitive régime it is regarded as proper to charge what the public is willing to pay; and why should a monopoly take any less? The fact would appear to be that in so far as trusts (or their managers) adopt a spirit of reasonableness it is because such a course is the one best calculated to secure for them the good will of the trade and of the consuming public, and thus to prolong their enjoyment of *moderate* monopoly profits.

(6) The trust because of inert management may not try to secure the maximum net profit. Unwilling to meet the attacks of competitors and of politicians, it may hesitate to exploit the public, and may rest satisfied with a moderate profit, perhaps little, if any, above a competitive level. Under these circumstances, the control of the business might soon be sought by more aggressive and forceful interests, alive to their opportunities, and able to make handsome returns even after paying a good price for the property. Yet the owners of the business, notwithstanding the inertness of the management, might refuse to sell, hence

there can be no certainty that each trust will be managed along the lines offering the maximum profit.

(7) A trust may fail to charge the price that produces the greatest net revenue through sheer inability to ascertain what that price is. Among the unknown factors in the problem are the amount of the demand at various prices and the extent to which the cost of production will increase or decline as the output varies. The matter is complicated because the demand schedule, even if it could be worked out for any given date, changes from time to time. The demand for any particular article depends on the state of business, on the mood of the consuming public, and on the distribution of purchasing power among the community. If business is good, the demand will normally be great, and a high price may yield the maximum net profit; and conversely, when a period of depression sets in. If the public is extravagantly minded, as at present (1919), a proportionately large outlay will be made for consumer's goods, and their monopoly price could well be high; and conversely for those articles that are in demand when thrift is in vogue. Again, if there occurs a marked change in the distribution of the community's purchasing power, so that the bondholders and the salaried classes have less and the working people more, the trusts that produce articles desired by those of increased purchasing power could raise their prices, whereas those trusts that produced articles desired by individuals of reduced purchasing power might be compelled to reduce their prices. There may be other matters that complicate the problem; but enough has been said to show that at best all that a trust can hope to do is to approximate the most profitable price. Though the price that it charges will doubtless be somewhat, perhaps considerably, above the competitive price, it will not be fixed, we may premise, as the result of a mathematical formula at the exact point that would actually prove to be the most remunerative.

The foregoing considerations make it evident that the price policy of the trusts has been less grasping than might have been expected of an agency formed largely for the express purpose of suppressing competition. They also demonstrate that though

there are certain forces at work to safeguard the public interest, these forces are not adequate of themselves, since they do not prevent the trusts from charging prices higher than the public would pay under competitive conditions, assuming that industry is as economically conducted under the latter state as under the first. As to legalizing trusts in the hope of satisfactorily regulating them and their prices, it will be shown in chapter XX that price regulation is a problem of the first magnitude and one whose successful solution is problematical.

CHAPTER XII

PROMOTERS' PROFITS IN THE ESTABLISHMENT OF TRUSTS

In this chapter it is proposed to indicate by a study of individual trust promotions the importance of promoters' profits as a cause contributing to the formation of trusts.

The function and work of the promoter have been well described elsewhere,[1] and need not be dwelt upon here in any detail. Briefly, in a typical trust promotion the promoter secured options on the plants that were to be combined; arranged, usually through an underwriting syndicate, for the raising of the necessary funds; organized a corporation to acquire the plants; and provided for the transfer of the plants (or securities) to the trust.

In effecting a trust promotion the promoter had first to obtain options on the properties (or the securities), otherwise the owners would in all likelihood have advanced their purchase price as it became evident that the trust was to be formed. The promoter, to be sure, might have bought all the properties for cash, but this would have involved a great deal of risk, and would, moreover, have been difficult to finance. In fact, it was rarely done. Second, he had to secure financial backing, since the trust required working capital (it did not ordinarily acquire the working capital of the constituent companies), and since some owners would almost certainly demand cash for their plants, refusing to accept securities, the value of which was more or less problematical.[2] Generally speaking, however, the amount

[1] See Meade, Trust Finance, chs. 4–6; Haney, Business Organization and Combination, ch. 18; and Lough, Corporation Finance, chs. 12–14.

[2] This cash the promoter usually secured through the sale of stock to an underwriting syndicate. Because of the risk that the stock could not be disposed of at a profit, the syndicate was wont to insist on a commission in the form of bonus stock.

of cash required to buy out the manufacturers was comparatively small. Ordinarily the promoter offered them at least one share of preferred stock and one of common stock in lieu of $100 in cash; [1] and tempted by the profits that were anticipated for the trust, the manufacturers commonly agreed to take the stock. Had they not been willing to take stock very few trusts would have been formed. The promoters would have been unable to supply the large amount of cash that would have been required,[2] and the public would have hesitated to buy securities that were unacceptable to the manufacturers, who were acquainted with the industry and its prospects. Third, the promoter had to organize a new company to acquire the plants or the stocks of the underlying companies, unless, indeed, one of the existing companies was used for this purpose. In any event the capitalization of the new (or reorganized) company was likely to be determined by the promoter, with the advice of the financiers. Finally, he had to arrange for the transfer of the properties or securities of the separate companies to the newly-organized corporation in exchange for its securities or for cash, or both. Sometimes the corporation gave to the promoter all or part of its stock in return for an agreement upon the part of the promoter to deliver to it the plants or control of the companies owning the plants. In that case the size of the promoter's profit depended on how favorable a bargain he was able to drive with the separate manufacturers. At other times the corporation offered to exchange its securities for those of the constituent companies at a definite ratio, the promoter taking his profit perhaps in the form of a stock commission. In either event there would probably be issues of stock to the financiers or bankers who agreed to supply the requisite funds.

It is clear, therefore, that the organization of a trust usually involved large issues of stock to a great variety of individuals. These included: (1) the promoters who purchased or secured

[1] The preferred stock usually represented the value of the plants; the common stock the anticipation of monopoly gains.

[2] The financiers would have balked, of course, at putting up cash to finance a proposition that the manufacturers mistrusted.

options on the properties, and who devised the financial plan; (2) the financiers who raised, or agreed to raise, the necessary funds; (3) the lawyers who incorporated the company, and attended to the legal aspects of the promotion; (4) the manufacturers who were generally unwilling to sell unless they received stock much in excess of the value of their properties; and (5) the public, which was expected to buy the stock, and which at times had to be tempted by an offer of common stock as a bonus. It frequently happened that the promoter was also a financier, that is, was a member of the underwriting syndicate, and less frequently perhaps he was also a manufacturer. His profits, therefore, were often a composite. Because of the difficulty, if not impossibility, of determining in individual cases of trust promotion to what extent the profits of the promoter were a reward for true promotion services, to what extent a reward for financial services, and to what extent for legal and miscellaneous services, we shall in general in this chapter use the term promoters' profits to indicate the profits made by the promoters, financiers, and lawyers, but not including those additional profits that were realized by these groups when they were also owners of stock in the companies that were combined. There can be no doubt that the promoter, when he was also a manufacturer, may have been animated fully as much by a desire to secure profits in the rôle of manufacturer as in the rôle of promoter, yet this motive was by no means always present, since many trusts were promoted by "outsiders." Under this use of the term promoters' profits, it will be observed, we are underestimating rather than exaggerating the importance of promoters' profits as an inducement toward the formation of trusts. However, it will still be true in many instances that the inducement remained sufficiently great to give a distinct fillip to the trust movement.

The largest trust and the one in which promoters' profits figured most prominently is the United States Steel Corporation. This company represented a union under the holding company plan of a group of concerns, some of which were merely combinations and others of which were trusts. The capitalization of

the Steel Corporation thus allowed for the remuneration of two sets of promoters, those that had organized the constituent companies of the Corporation, and those that organized the Corporation itself. The two cases will be described separately.

Some idea of the profits secured by the promoters of the steel combinations and trusts of 1898 to 1900 may be gained by an examination of the table on page 287, showing the amount of stock representing promotion charges, the value of this stock based on average market quotations during 1899 to 1900, and the percentage that this stock was of the total issue.[1] It should be noted that the amount of stock left in the hands of the promoters was not all profit, since usually the promoters had to give a part of this stock (or cash) to meet certain expenses incurred in the promotion. In general, however, such expenses were small.

Even a cursory examination of the table makes it clear that the promoters' profits were enormous. The promoters of the eight concerns for which data were available retained as their reward for promotion services some $63,000,000 of stock, or over one-tenth of the total issued stock (if we excluded the Carnegie Company, in the organization of which there were no promoters' profits, the ratio would be more than one-eighth). The market value of this stock, based on the average quotations during 1899 to 1900, was over $28,000,000. Its value based on the highest quotations of the respective securities during this same period was $40,549,188, and based on the lowest quotations, was $19,829,959. While the promoters could not have unloaded all of their stock at the highest quotation, it is improbable that they would have sold at the mininum figure for the two year period. If we assume that the promoters disposed of all their stock prior to 1901, the profits of promotion were at least $20,000,000;[2] if we assume that they did not

[1] Report of the Commissioner of Corporations on the Steel Industry, part I, pp. 126, 129, 133, 136, 138, 140, 144, 145, 170, 176–179. Referred to hereafter in this chapter as Report on the Steel Industry.

[2] These are pure profits of promotion; they do not include such indirect profits as the promoters might have made through the sale of securities given

Company	*Common stock representing promotion charges*	*Value based on average market price during 1899–1900* [1]	*Ratio of stock representing promotion charges to issued capital stock (including preferred)*
National Tube Co.	$20,000,000	$ 9,744,000	25.0
American Steel and Wire Co.	11,600,000	5,958,160	12.9
American Tin Plate Co.	10,000,000	3,477,000	21.7
American Bridge Co.	7,250,000	3,181,300	11.9
National Steel Co.	5,000,000	2,083,500	8.6
American Steel Hoop Co.	5,000,000	1,605,500	15.1
Federal Steel Co.	4,456,811 [2]	2,455,972	4.5
American Sheet Steel Co.	[3]		
Shelby Steel Tube Co.	[4]		
Carnegie Co.	none [5]		
Total	63,306,811	28,145,432	10.1 [6]

dispose of all of their stock—we know that they did not—their possible profits were much greater, since upon the organization of the Steel Corporation they were allowed to exchange their old stock for a greater amount of stock in the Corporation.[7] In any event the profits were sufficiently large to tempt daring promoters to take advantage of an opportunity to "get rich quick,"

to them in return for cash or in return for the securities that they held in the companies that were combined.

[1] In the case of companies not organized until late in 1899 or early in 1900 quotations are from the date of organization to the close of 1900.

[2] Includes $857,192 of preferred stock.

[3] Amount unknown, but probably large. See Report on the Steel Industry, part I, pp. 140, 178.

[4] Amount unknown, but apparently small. See ibid., pp. 144, 179.

[5] See ibid., p. 179.

[6] 13.5 per cent if we did not include the capital stock ($160,000,000) of the Carnegie Company.

[7] Except in the case of the American Steel Hoop Company and the American Sheet Steel Company.

whether or no the product of their daring subsequently demonstrated its fitness to survive in a business world that is harassed under normal conditions by the pressure of new capital seeking investment.

The promoters' profits realized in these early combinations and trusts in the steel industry, large as they were, were eclipsed by those obtained by the promoters of the United States Steel Corporation. The syndicate which undertook to secure a majority of the stock of the eight companies originally acquired by the Corporation incurred cash expenses of $28,000,000, of which amount $25,000,000 went to the Corporation for working capital. In return for this outlay and its underwriting services the syndicate was given by the Corporation a total of 1,299,975 shares of stock (half preferred and half common), having a par value of $129,997,500. On this stock the syndicate realized about $90,500,000.[1] Deducting the cash expenditures ($28,000,000), it is evident that the syndicate made a profit of $62,500,000. Of this amount one-fifth went to the firm of J. P. Morgan and Company, the syndicate managers, for their services; and the balance ($50,000,000) was distributed among the members of the underwriting syndicate, including the Morgan firm.[2] It is hardly necessary to point out that the possibility of making such large profits constitutes, in itself, a distinct inducement to the formation of trusts.

This huge compensation to the syndicate was, according to the Bureau of Corporations, greatly in excess of a reasonable payment; and particularly so in view of the reserved right of the syndicate managers to abandon the transaction at their own discretion.[3] The syndicate merely undertook to acquire the securities of various steel companies; it did not guarantee to do so. It should be noted, moreover, that while the syndicate subscribers stood liable to raise $200,000,000 upon request of the syndicate managers, it was generally understood that they would not be called upon for more than $25,000,000 in cash;

[1] Report on the Steel Industry, part I, p. 244.
[2] Ibid., pp. 244, 248.
[3] Ibid.,pp. 245–246.

and this, in fact, was all that they contributed, except some $3,000,000 for organization expenses. The Bureau of Corporations, in fact, alleged that this "large nominal obligation of the syndicate subscribers to the syndicate managers apparently was determined upon in part with a view to disarming subsequent criticism of the enormous compensation which it received."[1]

From the point of view of the public it is clear that it would be necessary to charge excessive prices for iron and steel products, if dividends were to be paid on the inordinate amount of stock given to the promoters of the Corporation, not to mention dividends on that part of the stock of the Corporation given to the promoters of the constituent companies (or their successors) in return for the stock held by them. The matter is important, since some $150,000,000 of the stock of the Corporation, or nearly one-seventh of its total stock, was issued, directly or indirectly, to promoters and underwriters.[2]

The American Tobacco Company (the cigarette trust) was organized in 1890 as a consolidation of five of the leading manufacturers of cigarettes. Since the manufacturers were themselves the organizers, there were no promoters' profits as we have employed the term. At that early date it was not common for trusts to be formed by "promoters"; and the number of manufacturers being so few, it was comparatively easy to arrive at an agreement. There was, however, a very marked overcapitalization in the organization of the trust. The capitalization of the company was $25,000,000, of which $15,000,000 was common stock and $10,000,000 preferred. The value of the assets acquired did not exceed $14,400,000.[3] The capitalization thus exceeded the assets (including good will) by at least $10,600,000. The establishment of a high degree of monopoly control, however, made it possible for the company to earn approximately 20 per cent on its common stock, water and all. Enormous profits were thus realized by the promoters of this

[1] Report on the Steel Industry, part I, pp. 245–246.

[2] See Report on the Steel Industry, part I, p. 251.

[3] Cf. p. 271.

company, but the profits were realized as manufacturers rather than as professional promoters.

The Continental Tobacco Company (the plug tobacco trust) was organized in 1898. This company was very heavily overcapitalized, but, as with the American Tobacco Company, nearly all of its securities went to the owners of the eleven plants that were combined. Inasmuch as five of these eleven plants belonged to the American Tobacco Company, and inasmuch as this concern had been conducting a severe competitive campaign to force its competitors into a combination, there was less occasion than usual for resort to a promoter, who should undertake the task of inducing the separate owners to combine their interests.

Though promoters' profits did not figure prominently in the organization of the plug tobacco trust, they were nevertheless present. The firm of Moore and Schley, well-known bankers and brokers, secured cash options on four important concerns, producing among them nearly one-quarter of the output that went into the trust in 1898.[1] The purchase price stipulated in the option agreements was $8,477,000. The bankers (Moore and Schley) also raised $2,751,400 in cash, to enable the Continental Company to take care of its promotion and other expenses.[2] For these properties and the cash the Continental Company gave $25,025,000 in stock (one-half preferred and one-half common), and $365,500 in cash.[3] The bankers in turn transferred $19,522,200 of the stock and all of the cash to the owners of the four plants; and retained as their pay $5,502,800 in stock, half preferred and half common. While the bankers doubtless incurred a few incidental expenses, it is substantially correct to say that their profits on the transaction were the realizable value of this stock minus the cash ($2,751,400) that

[1] Report of the Commissioner of Corporations on the Tobacco Industry, part I, p. 99; part II, p. 107.

[2] Report on the Tobacco Industry, part I, pp. 101–102.

[3] Ibid., part II, p. 107. The cash payment represented interest on the purchase price during the period that intervened between the signing of the option and the transfer of the plants to the Continental Company.

they raised. The market value of this stock during the three years of the life of the company—a reorganization was effected in 1901—based on the minimum and maximum quotations ranged between $2,476,260 and $5,370,732. On this basis, had they sold at the minimum quotations (which is quite unlikely) they would have sustained a loss of $275,140; had they sold at the maximum quotations (which is equally unlikely) their profits would have been $2,619,332.[1] On the other hand, if they refrained from selling during 1899–1901 they would have been in a position to participate in the reorganization of 1901 (when the American Tobacco Company and the Continental Tobacco Company were combined), in which event new opportunities for profit would have presented themselves. It is probable, therefore, that the bankers made a handsome profit; but it is certain that the possibility of realizing a profit for the promoters as such had little to do with the organization of the plug tobacco trust.

The syndicate of bankers and manufacturers that secured an option on the Liggett and Myers Tobacco Company, the largest plug tobacco concern outside of the trust, also made a large profit through its sale to the Continental Tobacco Company; in fact, it acquired the Liggett concern largely for that purpose. Yet since this syndicate, though composed in large measure of financial and banking interests, was the actual owner of the properties that it conveyed to the trust, its gains may not be regarded as true promoters' profits, but rather as profits received as an owner of property that was indispensable to the trust.

In addition to the cigarette and plug tobacco trusts a number of other companies with monopolistic aspirations were formed in the tobacco industry. These include the American Snuff Company (1900); the American Cigar Company (1901); the Consolidated Tobacco Company (1901); and the new American Tobacco Company (1904). In not one of these combinations, however, does it appear that any stock went to promoters or bankers for promotion services. The absence of promoters' profits in the organization of the first two of these combinations was probably

[1] Neglecting dividends and carrying charges in each case.

due to the fact that the concerns that were combined were so few in number that the owners were able to come together and effect an agreement among themselves; and in the last two to the fact that these combinations represented largely a rearrangement of securities, no new concerns being immediately brought in. On the whole, therefore, it is correct to say that promoters' profits have had surprisingly little to do with the formation of trusts in the tobacco industry.

The American Can Company (the tin can trust) was organized in 1901 with an issued capital stock of $82,466,600, half preferred and half common. Of this stock $78,000,000, equally divided between preferred and common stock, was given to the promoters in exchange for some ninety-five plants on which the promoters held options and for $7,000,000 in cash raised by them.[1] The promoters paid for the plants about $23,500,000, either in cash or in securities practically the equivalent of cash.[2] Thus, when the manufacturers took stock—most of them did, for otherwise the combination could not have been formed—they received one share of preferred and one share of common for each $100 of the purchase price. On the assumption that all of the manufacturers took stock, the promoters gave some $47,000,000 in stock for the plants, and had $31,000,000 left.[3] Of this amount about $14,000,000 might properly be regarded as payment for the $7,000,000 in cash turned over to the American Can Company as working capital. Their actual profits, therefore, were the realizable value of $17,000,000 in stock, half preferred and half common. How much the promoters actually realized there is no means of knowing, but the market value of this $17,000,000 in stock during April to August, 1901, was seldom below eight

[1] Petitioner's Summary of Evidence in United States *v.* American Can Company (no. 40), pp. 73–76.

[2] 230 Fed. Rep. 859.

[3] On the assumption that one share of preferred and one share of common were equivalent to $100 in cash it was immaterial to the promoters whether the manufacturers took cash or stock. If the manufacturers did not want stock the promoters had that much more cash to raise, but they retained that much more stock. Their profits would not be affected so long as the underlying assumption held good.

and one-half million dollars, and at times was considerably above. It is not intended to say that the promoters could have disposed of their stock during these months and have realized $8,500,000; for the sale of some 40 per cent of the total stock of the company during a comparatively short period would doubtless have led to a decline in its market value. Yet it is likely that around $8,000,000 could have been realized; and for this sum practically all of the plants could have been duplicated.[1] Whether the promoters in fact realized as much as $8,000,000 depends on how much confidence they had in the creature of their creation. The greater their confidence, the less their profits,[2] since by the fall of 1901 the bubble was pricked. Tin can prices, which had steadily advanced in the months following the organization of the American Can Company, soon took a decided drop, and with them went stock market quotations.

The International Harvester Company (the harvester trust) was organized in 1902 as a consolidation of the five principal manufacturers of harvesting machines. Its promotion was notable for the comparative absence of promoters' profits or even of overcapitalization. The total capitalization of the International Harvester Company at its organization was $120,000,000, all common stock. This stock was allotted as follows: [3]

For physical property of the five concerns (including bills receivable of the Milwaukee Company) [4]	$56,441,055
For bills receivable and cash of the other four manufacturing interests	49,851,803
For cash ($10,000,000) raised by the bankers	10,000,000
For organization expenses	749,999
For commission to the bankers	2,957,143
Total stock issue	$120,000,000

Of the total capital stock nearly half ($56,441,055) was issued

[1] 230 Fed. Rep. 870–871.

[2] Unless indeed they held their stock for a number of years.

[3] Calculated from a table in the Report of the Commissioner of Corporations on the International Harvester Company, p. 86.

[4] The Milwaukee Harvester Company was purchased as a going concern.

in return for the physical properties of the five companies (including bills receivable in the case of the Milwaukee company). The value of these properties as appraised by the organizers was approximately $67,000,000; as determined by the Bureau of Corporations only about $49,000,000.[1] Neither of these valuations, however, made any allowance for good will. It is clear, therefore, that the purchase price was substantially reasonable. Another block of the stock ($49,851,803) went to the McCormick, Deering, Plano, and Warder interests in exchange for cash subscriptions. In considerable measure these cash subscriptions took the form of an assignment to the International Harvester Company of bills receivable guaranteed by the vendor companies; but a considerable amount of cash was raised in addition.[2] The bills receivable being guaranteed, there was no stock inflation on this score.

The balance of the stock ($13,707,142) went to J. P. Morgan and Company, the bankers. This sum, it should be observed, does not include the $3,148,197 of stock given to the bankers in exchange for the Milwaukee Harvester Company, which was acquired by the bankers on behalf of the combination, and for which the bankers received stock equal to the actual value of the company as a going concern. What service did the bankers perform in return for this large issue of stock? In the first place, they agreed to subscribe to $10,000,000 of the stock of the company at par.[3] In the second place, they incurred certain expenses in the formation of the company. These expenses, amounting to $749,999, were covered by a specific allotment of stock, which is included in the $13,707,000. The balance of the stock received by them ($2,957,143) represented therefore their commission as bankers. Was this commission excessive? The Bureau of Corporations maintained that it was. It pointed out

[1] Cf. p. 236.

[2] Report on the International Harvester Company, p. 77. Companies selling harvesting machines have unusually large bills receivable because of the necessity of granting long terms of credit.

[3] They originally agreed to raise $19,000,000, but the amount was later reduced to $10,000,000.

that since this payment to the bankers did not correspond to any property conveyed or expenses incurred, it could be justified from the point of view of the company only on the ground of merger value—which did not materialize in the early life of the company—or on the ground of the value of an alliance with the firm of J. P. Morgan and Company.[1] Even on this score, that is, disregarding the welfare of the public, it held the payment to be excessive. As bearing on this matter it should be borne in mind that the risk of the bankers was comparatively slight. The bankers acted largely as the agents of a very small group of manufacturers, who were anxious to effect a combination, and who were in a position to deliver the requisite properties, since the stock of the companies was closely held. Moreover, the bankers assumed no obligations as underwriters, since payment for the properties was taken by the manufacturers in the form of stock. The main contribution of the bankers, therefore, outside of the purchase of the Milwaukee Company and the organization of the Harvester Company (for which services they were specifically remunerated) was the raising of $10,000,000. For this cash they did not, as was common in trust promotions, receive $200 in stock for each $100 in cash; they merely received stock dollar for dollar. The vital question, therefore, is: what was the value of the stock for which they subscribed at par? Was it anticipated that the organization of the trust would result in increased profits? In that case their commission was undoubtedly excessive. On the other hand, was there danger that the stock would fall below par? In that event their commission may have been distinctly moderate. The Report of the Bureau of Corporations did not discuss this question, and the lack of quotations for the company's securities during the early years makes it difficult to return a satisfactory answer. The fact is, however, that the profits of the Harvester Company during its early years were rather low, and its dividend payments distinctly low. It would appear, therefore, that the bankers did take considerable risk. It is conceivable that the company might have been able to avoid the issuance of the $3,000,000 of stock

[1] Report on the International Harvester Company, pp. 127–128.

that represented the bankers' commissions by the sale of $10,000,000 of stock at par to the public (which ordinarily receives no commission), but in view of the fact that a great mass of undigested trust securities was then hanging over the market this is by no means certain. In any event, it is clear that the promoters' profits in the formation of the harvester trust were distinctly small as compared with the other trusts of its size that were organized during the same period.

The profits of the promoters of a number of other trusts will be briefly reviewed. Unless stated to the contrary it should be understood in each instance that these profits are subject to some deductions for promotion expenses. They do not ordinarily, therefore, represent net profits.

The promoter of the starch trust (1890) secured options on a number of plants and raised $1,545,750. In return he received securities (bonds and stocks) that had an average market value during the first two years of the company's life of $2,268,427. His nominal profits, therefore, were $722,677.[1]

The promoters of the rubber boot and shoe trust (1892) received $1,300,000 of common stock, which at the average quotations during the first year had a value of approximately $560,000. Out of this sum the promoters had to meet organization expenses, but unlike many promotions their risk was small, since the amount of stock they received did not depend on their skill as bargainers, but was a definite percentage (5 per cent) of the total issue of stock.[2]

The promoters and financial backers of the glucose trust (1897) raised $4,500,000 in cash; and were given approximately $14,500,000 in securities, or over 38 per cent of the total issue. The average market value of this stock was $9,000,000; and the paper profit was therefore $4,500,000.[3]

The promoters of the malt trust (1897) received $500,000 in preferred stock and $7,750,000 in common stock (or nearly one-third of the total capitalization) to cover the expenses of promo-

[1] Dewing, Corporate Promotions and Reorganizations, pp. 53–55.

[2] Industrial Commission, XIII, pp. 48–49.

[3] Dewing, op. cit., p. 82.

tion. These securities were worth nearly $3,400,000 at their maximum quotations, but they declined rapidly and as a result most of the promoters made but slight profits.[1]

The promoters of the silver-ware trust (1898) received only $600,000 of common stock (equal to 3 per cent of the total capitalization), and out of this they had to meet the expenses of organization.[2] The market value of this stock during the first year was only about $100,000. It is clear, therefore, that the profit was small.

The promoters of the asphalt trust (1899) took their pay in considerable measure through the sale to the trust at fancy prices of a company which they organized for that particular purpose.[3] The properties of this company cost them $618,000; and they sold them to the trust of their creation for $3,670,000 in bonds, or more than five times their cost. In addition, as manufacturers they received bonds exceeding by nearly $2,500,000 the value of the properties transferred to the trust. Their profits as promoters were thus the realizable value of some $3,000,000 of bonds. The average price at which these bonds first sold was around $93, but the promoters could not have sold all of their bonds at this price without spoiling the market. There can be little doubt, however, that their profits were handsome.

The promoter of the bicycle trust (1899) after effecting the requisite transfer of securities for properties retained as his compensation $2,000,000 in debenture bonds, $2,600,000 in preferred stock, and $6,700,000 in common stock, or a total of $11,300,000 (equal to 31 per cent of the company's capitalization). This does not include such profits or losses as might have been made by the underwriting syndicate which supplied the requisite funds in return for bonds at 92½ cents on the dollar. Notwithstanding the fact that most of the manufacturers attested their faith in the company by taking securities, the promoter, because of the sudden collapse of the industry, realized only a small profit.[4]

The promoters and bankers that organized the cotton yarn

[1] Dewing, op. cit., pp. 276, 279.
[2] Industrial Commission, I, p. 1068.
[3] Dewing, op. cit., pp. 428–430.
[4] Ibid., pp. 253–254.

trust (1899) received nearly all the common stock ($5,000,000). The consolidation did not prove successful, and as a result the promoters realized no profit at all.[1] Substantially the same was true of the cotton duck trust, organized in 1901. The promoters of this trust after meeting the initial organization expenses had left $6,250,000 of common stock, of a value of at least $1,500,000. Having confidence in the company they not only retained this stock, but bought more; and in the end they sustained heavy losses.[2]

In the promotion of the foregoing trusts promoters' profits figured more or less prominently. In the organization of a number of other trusts, however, promoters' profits were insignificant or even entirely absent. This appears to be true of the oil, powder,[3] sugar, cash register, cordage, leather, aluminum, wall paper, shoe machinery, news print paper, glass table ware, and salt trusts. In the formation of some of these trusts, notably the sugar trust, large profits were made by the organizers, but these profits came to them as the owners of stock rather than as promoters. In the formation of others, notably the cordage and leather trusts, there was some underwriting of securities, but this was a detail in the formation of the trust rather than an important contributing cause. How, it may be asked, was it possible to organize this large number of important trusts without offering large rewards to the promoter, who is supposed to perform a necessary function? The answer is two-fold: (1) some trusts became such through the expansion of a concern already in the field, rather than through a combination at one time of most of the plants in the country. For instance, the Standard Oil Company, organized in 1870 to take over the business of the partnership to which it succeeded, bought first this property and then that, financing these purchases partly out of its enormous earnings, partly out of cash subscribed by the stockholders, and partly by an exchange of securities. Obviously no trust promoter was re-

[1] Dewing, op. cit., p. 313.

[2] Ibid., p. 341.

[3] There were large promoters' profits in the reorganization of this trust in 1902; but none in the original organization.

quired to create a trust developed in this fashion. (2) Some trusts, the news print paper trust, for example, were established with the aid of promoters who took no pay for their services. Their willingness to perform the service—they incurred no risk—may have been because they anticipated that the gain to them as manufacturers would be sufficient; or it may have been because they regarded the task as an opportunity to be of service to their trade, and the honor as a sufficient reward.

As a result of the foregoing study the conclusion would appear to be abundantly justified that the prospect of securing promotion profits has contributed markedly toward the formation of numerous trusts. It played a lesser part, however, than the hope of achieving monopoly prices. A number of trusts, as we have seen, were organized without promoters' profits; whereas few, if any, were organized without the anticipation at least of monopoly gains.

CHAPTER XIII

THE COMMON LAW RELATING TO COMBINATIONS AND TRUSTS[1]

The law relating to combinations and trusts is of two kinds—first, common law, and second, statute law. Statute law, in turn, may be either that of the states or of the federal government. Though we are concerned in this treatise mainly with the development of statute law (and particularly of federal law), a brief consideration of the common law decisions of the courts will be advantageous, especially since the Supreme Court in the Standard Oil case held that the term "restraint of trade" as used in the Sherman Act should be construed as declaratory of the common law on this subject.[2] Common law, it may be said, imports a system of unwritten law, not evidenced by statute. Its sources are found in the usages, habits, manners, and customs of a people; its seat, in the breast of the judges who are its expounders.[3] Common law yields to statute law, where such exists, yet until the late eighties there were very few state statutes dealing with industrial combinations and trusts, and until the passage of the Sherman Act in 1890 there was no federal statute. It was therefore only to be expected that a considerable body of common law doctrine had developed with respect to restraints of trade and combinations of one type or another.

The rule was early established in English law that contracts or agreements in restraint of trade were void, and therefore non-

[1] On this topic see the Report of the Commissioner of Corporations on Trust Laws and Unfair Competition, chs. 2, 7; and Goodnow, Trade Combinations at Common Law, Political Science Quarterly, 12, pp. 212–245. The author has made liberal use of these works in preparing this chapter.

[2] Cf. remarks of Senator Hoar in Cong. Record, April 8, 1890, p. 3152.

[3] Judicial and Statutory Definitions of Words and Phrases, second series, p. 810.

enforceable. The courts refused to recognize the validity of any restraint of trade, no matter how limited its scope. The cases which came before them in the early days involved principally the right of an individual, in disposing of his business, to agree not to reënter that same business. The courts took the position that in the interest of trade an individual should not be allowed to contract that he would stay out of the business in which he had been engaged. Subsequently, however, this rule was relaxed. In *Mitchell* v. *Reynolds* (1711) an English court held that while general restraints of trade were void, a restraint limited to a particular place might under certain circumstances be enforceable.[1] Though American courts, following *Mitchell* v. *Reynolds*, have in many cases held that an agreement involving a restraint covering an entire state is void as a general restraint,[2] still the cases are numerous in which American courts have upheld particular restraints when the restraint was regarded as reasonable.[3] The modern rule was well stated in *Hubbard* v. *Miller*. "If, considered with reference to the situation, business and objects of the parties, and in the light of all the surrounding circumstances with reference to which the contract was made, the restraint contracted for appears to have been for a just and honest purpose, for the protection of the legitimate interests of the party in whose favor it is imposed, reasonable as between them and not specially injurious to the public, the restraint will be held valid."[4] Gradually, therefore, the principle became established at common law that agreements connected with the sale of a business were not necessarily void, even though thereby a restraint of trade was effected, providing the restraint was reasonable in character.

[1] 1 P. Wms. 181 (1711).

[2] See Lawrence *v.* Kidder, 10 Barbour (New York) 641 (1851); Taylor *v.* Blanchard, 95 Massachusetts 370 (1866); Western Woodenware Association *v.* Starkey, 84 Michigan 76 (1890).

[3] See Bowser *v.* Bliss et al., 7 Blackford (Indiana) 344 (1845); Duffy *v.* Shockey, 11 Indiana 70 (1858); Beal *v.* Chase, 31 Michigan 490 (1875); Whitney *v.* Slayton, 40 Maine 224 (1885); Diamond Match Company *v.* Roeber, 106 New York 473 (1887); Robinson *v.* Suburban Brick Company, 127 Fed. Rep. 804 (1904).

[4] 27 Michigan 19 (1873).

AGREEMENTS TO RESTRICT COMPETITION

The next class of cases to be described (we are following here the classification adopted in the report of the Commissioner of Corporations on Trust Laws) is that relating to agreements among competitors to restrict competition or to form a combination, but not including such restriction of competition as results from the formation of a trust. The latter will be described later.

Agreements to restrain competition, as pointed out in the chapter on Pools, may be of various sorts. They may be informal, as, for example, the gentlemen's agreements, or they may be quite formal, with provisions for penalties in the event of a failure to observe the agreement. The agreements may look toward the control of the supply, the limitation of the output, the fixing of prices, the pooling of profits, or the division of territory. Whatever their form, they were void under the common law when they unduly restrained competition, and were therefore detrimental to the public interest. No rule for the determination of what constituted undue restraint under the common law was laid down; the common law doctrine was that each case should be settled in the light of the facts.

The state of the common law can best be indicated by citing a few representative cases, some of them illustrating invalid agreements, and some valid agreements.

Invalid Agreements [1]

India Bagging Association v. *B. Kock and Company.*[2] Eight firms had formed an association for the sale of India bagging,

[1] See also Craft *v.* McConoughy, 79 Illinois 346, (1875); Arnot *v.* The Pittston and Elmira Coal Company, 68 New York 558 (1877); Santa Clara Valley Mill and Lumber Company *v.* Hayes, 76 California 387 (1888); Anderson *v.* Jett, 89 Kentucky 375 (1889); Samuels *v.* Oliver, 130 Illinois 73 (1889); Emery *v.* Ohio Candle Company, 47 Ohio State 320 (1890); Strait *v.* National Harrow Company, 18 New York Supplement 224 (1891); The Texas Standard Oil Company *v.* Adoue, 83 Texas 650 (1892); Oliver *v.* Gilmore, 52 Fed. Rep. 562 (1892); Bohn Manufacturing Company *v.* Hollis,

[2] 14 Louisiana Annual Reports 168 (1859).

the bagging to remain the property of the individual members. Each firm agreed not to sell any bagging for a period of three months, except with the consent of the majority, under a penalty of $10 for every bale sold. The manager of the association brought suit against one of the members for having sold 740 bales of bagging, in contravention of the articles of the association. The Court held that the agreement entered into was palpably and unequivocally a combination in restraint of trade, and to enhance the price of an article of primary necessity to cotton planters; and that it was contrary to public order, and might not therefore be enforced in a court of justice.

Morris Run Coal Company v. *Barclay Coal Company.*[1] Five coal companies in Pennsylvania had entered into an arrangement in New York by which they agreed to divide among themselves in certain proportions the market for the bituminous coal produced in the two coal regions controlled by them; and to appoint a committee to take charge of their business. The committee was empowered to adjust the prices of coal in the different markets, and the rates of freight, and to enter into agreements with the anthracite coal companies. Provision was made for the mining of coal and its delivery in the different markets at such times and to such parties as the committee might direct, and for the sale of the coal through a general sales agent to be appointed by the committee, and to be stationed in New York state. However, the companies were allowed to sell the coal themselves, provided they did not exceed the proportion allotted to them, and provided they sold at the prices fixed by the committee. In an action on a draft, given in furtherance of the agreement, the Court held that the contract was void under the common law, being in restraint of trade and against public policy. It was also held to be void on the ground that

54 Minnesota 223 (1893); Nester *v.* Continental Brewing Company, 161 Pennsylvania State 473 (1894); Charleston Natural Gas Company *v.* Kanawha Natural Gas, Light and Fuel Company, 58 West Virginia 22 (1905); Pocahontas Coke Company *v.* Powhatan Coal and Coke Company, 60 West Virginia 508 (1906).

[1] 68 Pennsylvania State 173 (1871).

it violated a New York statute prohibiting conspiracies to commit an act injurious to trade or commerce.

The Central Ohio Salt Company v. *Guthrie.*[1] Practically all the salt manufacturers in the Hocking and Muskingum valleys, Ohio, had formed a voluntary association for the express purpose of regulating the price, and sustaining the quality of salt. By the articles of association, all salt manufactured or owned by the members became the property of the Central Ohio Salt Company as soon as it was packed into barrels. The members of the association were then prohibited from selling any salt except by retail at the factory, and except at prices fixed by the company. The proceeds of sales were turned over to the members in proportion to the amount of salt received from each. For some time after the organization of the association the defendant complied with the agreement, but subsequently he refused to deliver to the company the output of his furnace. Whereupon the Central Salt Company brought suit to enforce the agreement.

The judge pointed out that while it was well settled that all contracts in *partial* [2] restraint of trade were not void as against public policy, it was as fully established that contracts in *general* [2] restraint were against public policy, and therefore absolutely void. "Public policy," ~~he said,~~ "unquestionably, favors competition in trade, to the end that its commodities may be afforded to the consumer as cheaply as possible, and is opposed to monopolies, which tend to advance market prices, to the injury of the general public." The Court held that the clear tendency of the agreement before it was to establish a monopoly, and to destroy competition in trade, and for that reason, on grounds of public policy, the Court would not aid in its enforcement. To say that competition in the salt trade was not destroyed, or that the price of the commodity was not unreasonably advanced was no answer; it was enough that the inevitable tendency of such contracts was injurious to the public.

Raymond v. *Leavitt.*[3] The plaintiff had lent the defendant

[1] 35 Ohio State 666 (1880). [2] Italics supplied by the author.
[3] 46 Michigan 447 (1881).

$10,000 for the purpose of controlling the wheat market at Detroit, the intent being to force up prices. The defendant was to give the plaintiff one-third of the profits, and at all events to repay the principal. The Court held that the object of the arrangement between the parties was to force a fictitious and unnatural rise in the wheat market for the express purpose of getting the advantage of dealers and purchasers. The Court declined to enforce such a contract. It held that if people saw fit to invest their money in such ventures, they must get it back by some other than legal measures.

De Witt Wire-Cloth Company v. *New Jersey Wire-Cloth Company.*[1] Five concerns engaged in the manufacture and sale of wire cloth entered into an agreement whereby, for the avowed purpose of regulating the price of wire cloth, they formed themselves into an association, agreed that they would not sell below stipulated prices, and subjected themselves to a heavy penalty for the violation of the agreement. The Court held that the inevitable effect of this agreement was to restrict competition in trade, and to enhance arbitrarily the price of a commodity of commerce; and it was a settled principle in the jurisprudence of this country that such a contract was repugnant to public policy, and thus unlawful. The Court held that the people had a right to the necessaries and conveniences of life at a price determined by the relation of supply and demand, and the law forbade any agreement or combination whereby that price was removed beyond the salutary influence of legitimate competition.

Chapin v. *Brown Brothers.*[2] The grocery men of Storm Lake, Iowa, finding the business of purchasing and retailing butter burdensome, and believing that the business could be handled more satisfactorily by one concern making this its exclusive affair, agreed with the firm of D. and E. Chapin that for a period of two years they would buy no more butter or take none in trade, except for the use of their own families. The Chapin firm in accordance with this agreement established a store in Storm

[1] 14 New York Supplement 277 (1891). [2] 83 Iowa 156 (1891).

Lake. Notwithstanding the agreement the defendants subsequently opened a butter store. The Chapin concern brought suit to enforce the agreement.

The Court refused to enforce the agreement on the ground that it lacked consideration, and that it was against public policy. The Court held that it plainly tended to monopolize the butter trade of Storm Lake, and to destroy competition in the business. By this decision an agreement against public policy was declared void, even though it applied to purchase rather than sale, and even though it resulted in no disadvantage to the consuming public generally, the parties injured being the producers of butter.

More v. *Bennett*.[1] The law stenographers of the city of Chicago had formed an association, the object of which was to establish and maintain uniform rates for stenographic work done by the members of the association. A schedule of rates had been drawn up, but it had not been observed by the defendant, so the plaintiff alleged. The Court, however, refused to award damages. It held that one of the leading objects of the association, if not its leading object, was to control the prices to be charged by its members by restraining all competition between them; and the agreement was thus so obnoxious to public policy as to render it improper for the courts to lend their aid to its enforcement. This decision is significant in that the Court applied the same rules to agreements regulating the price of labor as were applied by the courts generally to agreements regulating the price of commodities.

The People of the State of New York v. *The Milk Exchange*.[2] The Milk Exchange had some ninety stockholders, most of whom were either milk dealers in the city of New York or creamery and milk commission men in the vicinity. At the first meeting after its incorporation it adopted a by-law which provided that the board of directors should have power to fix the price at which milk was to be purchased by the stockholders. The directors accordingly fixed the price of milk from time to

[1] 140 Illinois 69 (1892).

[2] 145 New York 267 (1895).

time, and the prices thus established largely controlled the market in New York and vicinity. The Attorney General of the state brought suit to have the charter of the company forfeited. The Court granted the relief requested. It held that the evidence justified a finding that the Milk Exchange was a combination inimical to trade, and thus unlawful. That the purpose of the combination may have been to reduce the price of milk made no difference. The price was fixed for the benefit of the dealers, not the consumers; and the logical effect of the fixing of prices by the combination was to paralyze the production and limit the supply, and thus to leave dealers in a position to enhance the price to be paid by consumers.

Slaughter v. *Thacker Coal and Coke Company*.[1] The Thacker Coal Company had been organized in 1895 for the sole purpose of acting as the sales agent of the Thacker Coal and Coke Company, and two other coal mining concerns. The Thacker Coal Company entered into a contract with the Thacker Coal and Coke Company, whereby it agreed to sell for the latter at least 20,000 tons of coal a year for five years, at a commission of 10 cents per ton. The Coal and Coke Company agreed to deliver to the selling corporation as much coal as the latter could sell, but not to exceed 84,000 tons a year. The mining concern agreed to pay 10 cents per ton as liquidated damages, should it fail to deliver coal according to the agreement. Selling prices were fixed in the agreement, and were not to be changed without the consent of the three producing companies. In 1896 the Thacker Coal and Coke Company refused to deliver any more coal under the contract. The receiver for the Thacker Coal Company thereupon brought suit against the Coal and Coke Company for damages. The Court pointed out that the modern rule at common law was that contracts in restraint of trade were enforceable, if they did not unreasonably restrain trade. But the contract before it, though relating to only an insignificant part of the coal produced in the state, was held to be illegal as tending to injure the public; and therefore no recovery could be had on it.

[1] 55 West Virginia 642 (1904).

Valid Agreements [1]

Skrainka v. *Scharringhausen.*[2] Twenty-four owners and operators of stone quarries in a section of St. Louis, desiring to effect a sale of their stone at "uniform prices and living rates," had entered into an agreement, which was to last for six months. The agreement made provision for the appointment of an exclusive sales agent, who was to apportion the output among the quarries and to sell the stone at specified prices. The defendant, who had violated the agreement, and thus incurred a penalty, contended that the agreement was in restraint of trade, and not enforceable at law. The Court pointed out that the old doctrine of the common law, declaring that contracts in restraint of trade were void, was no longer to be insisted upon as rigorously as it had been in the earlier cases. Every agreement in restraint of trade was no longer illegal. When a contract injured the parties making it, by diminishing their means for supporting their families; when it tended to deprive the public of the services of useful men; when it discouraged industry, diminished production, prevented competition, enhanced prices, and when, being made by large companies or corporations, it excluded rivalry and engrossed the markets—that is, tended to "make a corner"—it was against the policy of the law. But restraints upon trade imposed by agreement, under limitations as to locality, time, and persons, were not necessarily restraints of trade in the general sense, and thus objectionable. Applying this principle to the case before it, the Court said, "The agreement is among the quarrymen of one district of one city, and it does not appear that it embraces all of them. There is no evidence that it works any public mischief, and the contract is not of such a nature that it is apparent from its terms that it tends to deprive men of employment, unduly raise prices, cause a monopoly, or put an end to competition. It is limited both as to time and place; and

[1] See also Long *v.* Towl, 42 Missouri 545 (1868); Gloucester Isinglass and Glue Company *v.* Russia Cement Company, 154 Massachusetts 92 (1891); and Matthews *v.* Associated Press, 136 New York 333 (1893).

[2] 8 Missouri Appeals Reports 522 (1880).

we know of no case in recent times in which a contract such as the one before us has been declared illegal."

Dolph v. *Troy Laundry Machinery Company*.[1] The plaintiff and the defendant were the two leading manufacturers of washing machines in the United States. In order to avoid the consequences of competition with each other, and to secure better prices and larger returns, they had entered into a five-year agreement to divide profits. The Dolph concern was to have the option of manufacturing all machines sold by both parties, and the Troy concern agreed to take a certain number of machines annually. The Troy concern having terminated the contract prior to its expiration, the Dolph concern brought suit to recover damages. The Court held the agreement valid. As its decision seems to have taken a different turn from the great majority of cases, we quote at some length.

"Assuming that, in entering into the contract, the parties contemplated that the defendant should cease manufacturing machines, and buy all its machines from the plaintiff, and that the only purpose in view was to promote the interests of the parties, and enable them to obtain from customers higher prices for the machines, it is not obvious how such a contract contravenes any principle of public policy. Washing-machines, although articles of convenience, are not articles of necessity. The scheme of the parties did not contemplate suppressing the manufacture or sale of machines by others. Those who might be unwilling to pay the prices asked by the parties could find plenty of mechanics to make such machines, and the law of demand and supply would effectually counteract any serious mischief likely to arise from the attempt of the parties to get exorbitant prices for their machines. It is quite legitimate for any trader to obtain the highest price he can for any commodity in which he deals. It is equally legitimate for two rival manufacturers or traders to agree upon a scale of selling prices for their goods, and a division of their profits. It is not obnoxious to good morals, or to the rights of the public, that two rival traders agree to consolidate their concerns, and that one shall discontinue business, and

[1] 28 Fed. Rep. 553 (1886).

become a partner with the other, for a specified term. It may happen, as the result of such an arrangement, that the public have to pay more for the commodities in which the parties deal; but the public are not obliged to buy of them. Certainly, the public have no right to complain, so long as the transaction falls short of a conspiracy between the parties to control prices by creating a monopoly."

Central Shade-Roller Company v. *Cushman.*[1] Three manufacturers of shade-rollers, each possessing different letters patent, had, for the purpose of avoiding competition, organized the Central Shade-Roller Company, and severally entered into an agreement with it that all sales of shade-rollers should be in the name of the Central Company, and should be at once reported to it. It was further provided in the agreement that the prices for rollers of the same grade should be the same, the price to be according to a schedule contained in the contract, subject to changes made by the company on the recommendation of three-fourths of the stockholders; and that when either party should establish an agency in any city for the sale of a particular roller, no other party should take orders for the same roller in the same place. The Central Shade-Roller Company alleged that the defendant had broken the contract, and prayed for an injunction to restrain the defendant from selling rollers in violation thereof.

The Court upheld the agreement. It held that the contract put no restraint upon the production or sale of shade-rollers; on the contrary its apparent purpose was, by making prices more uniform and regular, to stimulate production. Moreover, the agreement did not refer to an article of prime necessity, nor to a staple of commerce, nor to merchandise to be bought and sold in the market, but to a particular curtain fixture of the parties' own manufacture. Finally, the agreement did not aim to affect competition from outside,—the parties had a monopoly by their patents,—but only to restrict competition in price among the members. Even if it were true that the agreement tended to

[1] 143 Massachusetts 353 (1887).

raise the price of the commodity, it was, nevertheless, one which the parties had a right to make. But the Court refused to assume that the purpose and effect of the combination was to raise unduly the price of the commodity. It held that its natural effect would be the maintenance of a fair and uniform price, and the prevention of the injury to producers and consumers resulting from fluctuating prices, in turn the result of undue competition. The question would be different, said the Court, if it appeared that the combination was used to the public detriment. The contract being apparently beneficial to the parties and not necessarily injurious to the public, the Court declined to hold it invalid as a restraint of trade, or against public policy.

It is doubtful whether the principle laid down in this case is sound. In United States *v.* Addyston Pipe and Steel Company, a federal court, discussing the shade-roller case, said that it was there held that contracts in restraint of trade are not invalid if they affect trade in articles which, though useful and convenient, are not articles of prime or public necessity. But "we think the cases hereafter cited show that the common law rule against restraint of trade extends to all articles of merchandise." [1]

"TRUSTEE DEVICE" CASES

We now come to the common law cases dealing with trusts. These trusts, as we have seen, at one time took the form of a "trust" agreement or a trustee device, but later took the form of a corporate combination. The cases declaring the "trust" agreement illegal will be first considered.[2]

Mallory v. *Hanaur Oil-Works*.[3] This was one of the first cases involving a "trust" agreement. In July, 1884, four corporations manufacturing cotton seed oil at Memphis, Tennessee, entered into a contract. They agreed to turn over to a committee, composed of representatives of each corporation, the properties and

[1] 85 Fed. Rep. 286 (1898).

[2] See also Pittsburg Carbon Company (Ltd.) *v.* McMillin, 119 New York 46 (1890); and Bishop *v.* American Preservers' Company, 157 Illinois 284 (1895).

[3] 86 Tennessee 598 (1888).

machinery of each mill. These properties were to be managed for the common benefit by the committee (it went under the name of the "Independent Cotton-Seed Association"); and the profits and losses were to be divided among the corporations according to definite proportions. This arrangement was to last one year, but it might be renewed for two additional years; and in fact was renewed at the end of the first year. Prior to the expiration of the agreement the Hanaur Oil-Works passed a resolution declaring the contract void, as being ultra vires, and directed its president to resume possession of the mill. The association refused to turn over the mill, whereupon suit was brought by the Hanaur Oil-Works to recover possession.

The Court held that the agreement entered into was a contract of partnership between corporations; that the Hanaur Oil-Works under its charter had no power to enter such a partnership; that the contract was therefore void; and that consequently the company might resume possession of its property. The Court did not deem it necessary to consider the question of the legality of such a combination of corporations as one tending to create a monopoly, though it pointed out that the question thus raised was a grave one.

State v. *Nebraska Distilling Company.*[1] The Nebraska Distilling Company had entered the Distillers and Cattle Feeders' Trust in 1887, but its plant, though it had formerly been operated at a profit, was closed by order of the trustees. Subsequently at a meeting of the stockholders of the Nebraska Distilling Company the directors were authorized to sell the company's property, to cancel all the stock outstanding, and to dissolve the corporation, The state thereupon brought suit to obtain a forfeiture of the corporate franchise of the company. The Court held that the object of the Nebraska Distilling Company in entering the illegal combination was to destroy competition, and create a monopoly; that any contract entered into with such an object was, under the laws of the state, null and void; that the conveyance from the distilling company to the trust was in contravention of the authority conferred by law

[1] 29 Nebraska 700 (1890).

upon that company, in excess of the powers granted by its charter, and against public policy and void; and that no title had passed by such conveyance. The Court further held that the corporate franchise, having been abused, would be annulled; and that the property of the Nebraska Distilling Company, being within the jurisdiction of the Court, would be disposed of in such manner as justice required.

The People of the State of New York v. *The North River Sugar Refining Company.*[1] The organization of the Sugar Refineries Company in 1887 has already been described.[2] In 1888 the Attorney General of New York brought suit against the North River Sugar Refining Company, alleging that the entry of the company into the trust justified the vacating of its charter.

The Court held it that could not be denied that the North River Sugar Refining Company had became an integral part of a combination which possessed over it absolute control. The defendants, however, alleged that this outcome was the result of action by the stockholders and not by the corporation, and that therefore the penalty of dissolution should not be visited upon the corporation. But the Court held that there might be actual corporate conduct without formal corporate action. It pointed out that the stockholders at a meeting had unanimously adopted a resolution favoring the establishment of the "trust", and had entered into an agreement to transfer their shares of stock to the trustees. The stockholders in acting collectively, as an aggregate body, without the least exception, had reached results clearly corporate in character, and they could not escape the consequence of their acts by pleading the innocence of a convenient fiction, that is, the corporation. It being established that the North River Sugar Refining Company had participated in the creation of the trust, it was next necessary to determine whether this was illegal. The Court held that it was clear that the defendant had accepted from the state the gift of corporate life only to disregard the conditions upon which it had been given; that it had received its powers and privileges merely to put them in pawn; that it had given away to an ir-

[1] 121 New York 582 (1890). [2] Cf. p. 22.

responsible board its entire independence and self-control. Its stockholders had parted with the control which the charter gave them and the state required them to exercise. And graver still was the fact that the corporation had helped to create an anomalous trust, which was in substance and effect a partnership of twenty separate corporations; and it was a violation of the law for corporations to enter into a partnership. The Court therefore declared that the charter of the company should be forfeited, and its corporate existence annulled. The Court indulged in a dictum as to the injurious effects of monopolies upon the public, but did not decide the case on that ground, holding that it was needless in this instance "to advance into the wider discussion over monopolies and competition and restraint of trade and the problems of political economy."

State v. *Standard Oil Company.*[1] We have already described at some length the Standard Oil "trust" agreement of 1882.[2] The Supreme Court of Ohio in a decision rendered in 1892 declared the agreement illegal. In a line of reasoning similar to that of the New York court in the North River Sugar Refining Company case, it held that the action of the stockholders of the Standard Oil Company in turning over their shares to the trustees provided for in the agreement had affected the property and business of the Standard Oil Company in the same manner as if it had been a formal resolution of the board of directors, and that their acts should be regarded as the acts of the corporation. And the nature of the agreement was such as to preclude the Standard Oil Company of Ohio from becoming a party to it. The law required that a corporation should be controlled and managed by its directors in the interests of its own stockholders, and conformable to the purpose for which it was created by the laws of the state. But by the agreement entered into the defendant was controlled and managed by the Standard Oil Trust, an association with its principal place of business in New York, and organized for a purpose contrary to the policy of the laws of the state of Ohio. "Its object was to establish a virtual monopoly of the business of producing petroleum, and of manufacturing, refining

[1] 49 Ohio State 137 (1892).

[2] Cf. p. 19.

and dealing in it and all its products, throughout the entire country, and by which it might not merely control the production, but the price at its pleasure. All such associations are contrary to the policy of our state and void." The Court therefore held that the Standard Oil Company should be forbidden to carry out the agreement which it had entered into with the "trust."

CORPORATE COMBINATION CASES

The last class of cases deals with the establishment of corporate combinations.[1] The first of these was:

Richardson v. *Buhl*.[2] The Diamond Match Company was organized in Connecticut in 1880 for the purpose of acquiring all the factories in the United States manufacturing friction matches, with the intent of monopolizing the business and controlling prices. The companies which went into the trust exchanged their real estate, machinery, patents, good will, and agreements not to reënter the match business for common stock in the Diamond Match Company; and agreed to buy preferred stock equal to one-half the amount of common stock received, the preferred stock to be paid for in matches or match materials on hand, or in cash. The Richardson Match Company not being in sufficient funds to buy the preferred stock, borrowed money from Buhl, and to secure the repayment of the loan endorsed the greater part of the preferred stock over to Buhl, with an agreement between the parties as to the division of the dividends received on the stock held as collateral. Suit was brought by Richardson in connection with this agreement.

The parties to the suit did not dispute the validity of the contract entered into, but the Court, on its own motion, raised the question. The Court held that the contract had been entered into to aid the Diamond Match Company in carrying out the object for which it had been organized,—the monopolization of the manufacture of friction matches in the United

[1] See also People *v.* Chicago Gas Trust Company, 130 Illinois 268 (1889); and Harding *v.* The American Glucose Company, 182 Illinois 551 (1899).

[2] 77 Michigan 632 (1889).

States. But monopoly in trade or in any kind of business, according to the Court, was odious to our form of government; its tendency was destructive of free institutions, and repugnant to the instincts of a free people. The Diamond Match Company being unlawful, and the contract in question having been made to further its objects and purposes, the contract was void as against public policy.

Distilling and Cattle Feeding Company v. *People.*[1] Reference has been made to the organization of the Distillers and Cattle Feeders' Trust in 1887.[2] In 1890, because of court decisions holding similar trusts illegal, the corporate form of organization was adopted. In 1893 the Attorney General of Illinois brought suit against the Distilling and Cattle Feeding Company (the corporation which succeeded the "trust"), alleging that the company had misused its powers and franchises.

The Court held that no one who intelligently considered the scheme of the Distillers and Cattle Feeders' Trust could for a moment doubt that it was designed to be, and was in fact, a combination in restraint of trade; and that it was organized for the purpose of getting control of the manufacture and sale of all distillery products, so as to stifle competition, and to be able to dictate output and prices, and thus to create or tend to create a monopoly. The "trust" was clearly against the policy of the law, and it was therefore illegal and void. And the corporation had merely succeeded to the trust. Its operations were to be carried on in the same way, for the same purposes, and by the same agencies as before. The former trustees became the directors of the new corporation, and the trust certificate holders became its stockholders. The trust being repugnant to public policy and illegal, it was impossible to see, said the Court, why the same was not true of the corporation which succeeded to it and took its place. The control over the distillery business of the country, over production and prices, and the virtual monopoly formerly held by the trust, were in no degree changed or relaxed. The Court concluded, "There is no magic in a corporate organization which can purge the

[1] 156 Illinois 448 (1895). [2] Cf. p. 21.

trust scheme of its illegality, and it remains as essentially opposed to the principles of sound public policy as when the trust was in existence. It was illegal before, and is illegal still, and for the same reasons." [1] The judgment of the court below ousting the company from its franchises was therefore affirmed.

The cases outlined in this chapter illustrate fairly the decisions of the courts of the country, which almost without exception have held illegal all agreements in unreasonable restraint of trade, and all monopolies or attempted monopolies, irrespective of the form in which they were clothed. The decisions of the courts declaring illegal the trust agreements in the cotton seed oil, whisky, sugar, oil, and preserving industries, and the corporate combinations in the match and whisky industries apparently left no loophole under the common law for the establishment of industrial monopolies.

We may now proceed to describe the federal legislation dealing with combinations and trusts, and the decisions of the courts interpreting this legislation.

[1] 156 Illinois 491.

CHAPTER XIV

TRUST LEGISLATION TO 1914 [1]

During the years 1882 to 1887 a number of trusts had been created. This movement toward industrial monopoly was viewed with great concern by the people of the United States, and a vigorous demand was made for the enactment of legislation that would definitely make these trusts illegal. As Justice Harlan said in 1911: "All who recall the condition of the country in 1890 will remember that there was everywhere, among the people generally, a deep feeling of unrest. The Nation had been rid of human slavery—fortunately, as all now feel—but the conviction was universal that the country was in real danger from another kind of slavery sought to be fastened on the American people, namely, the slavery that would result from aggregations of capital in the hands of a few individuals and corporations controlling, for their own profit and advantage exclusively, the entire business of the country, including the production and sale of the necessaries of life." [2] In 1888 both of the leading political parties referred in their platforms to the dangers inherent in trusts, and demanded action. Thus, the platform of the Republican party read:

"We declare our opposition to all combinations of capital, organized in trusts or otherwise, to control arbitrarily the condition of trade among our citizens; and we recommend to Congress and the state legislatures, in their respective jurisdictions, such legislation as will prevent the execution of all schemes to oppress the people by undue charges on their supplies, or by unjust rates for the transportation of their products to market." [3]

[1] For a more detailed account of the legislation of this period, see Knauth, The Policy of the United States towards Industrial Monopoly.

[2] 221 U. S. 83.

[3] McKee, The National Conventions and Platforms of all Political Parties, p. 241.

The Democratic party platform held that "the interests of the people are betrayed when, by unnecessary taxation, trusts and combinations are permitted to exist, which, while unduly enriching the few that combine, rob the body of our citizens by depriving them of the benefits of natural competition." [1] In the same year investigations of trusts were provided for by the House of Representatives and by the state of New York; and numerous bills dealing with combinations and trusts were introduced in the United States Senate. The opposition to trusts crystallized in 1890 in the passage on July 2 of the Sherman Anti-trust Act,—as it is generally called.

The course of the act through Congress has been described elsewhere,[2] and only a brief sketch need be given here. The bill was introduced in the Senate by Senator Sherman of Ohio on December 4, 1889. It was debated on February 27, March 21, March 24–27, and April 8, 1890. During the course of the debate Senator George stated his belief that "the sentiment that something ought to be done pervades this body almost universally;" [3] and it is significant as supporting this view that only one speech in opposition to anti-trust legislation was delivered in the Senate.[4] Having been revised so completely that it bore little resemblance to the original measure, the bill passed the Senate on April 8, by a vote of fifty-two to one, twenty-nine being absent.[5] On May 1 the bill was taken up in the House, and after a short debate was passed with one amendment, the votes not being recorded.[6] The House amendment did not prove acceptable to the Senate, and accordingly a conference became necessary. Eventually on June 20 by a vote of 242 to 0, 85 not voting, the House agreed to withdraw its amendment.[7] The

[1] McKee, The National Conventions and Platforms of all Political Parties, p. 235.

[2] Walker, History of the Sherman Law, chs. 1–2, and Knauth, The Policy of the United States towards Industrial Monopoly, ch. 1.

[3] Cong. Record, March 25, 1890, p. 2598.

[4] Ibid., March 24, 1890, pp. 2565–66.

[5] Ibid., April 8, 1890, p. 3153.

[6] Ibid., May 1, 1890, p. 4104.

[7] Ibid., June 20, 1890, p. 6312.

bill was signed by President Harrison on July 2; and in its final form was identical with the measure as it had passed the Senate on April 8.

The provisions of the act may be briefly summarized (the text is given in a footnote).[1]

[1] An act to protect trade and commerce against unlawful restraints and monopolies.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

Sec. 1. Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations, is hereby declared to be illegal. Every person who shall make any such contract or engage in any such combination or conspiracy, shall be deemed guilty of a misdemeanor, and, on conviction thereof, shall be punished by fine not exceeding five thousand dollars, or by imprisonment not exceeding one year, or by both said punishments, in the discretion of the court.

Sec. 2. Every person who shall monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several States, or with foreign nations, shall be deemed guilty of a misdemeanor, and, on conviction thereof, shall be punished by fine not exceeding five thousand dollars, or by imprisonment not exceeding one year, or by both said punishments, in the discretion of the court.

Sec. 3. Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce in any Territory of the United States or of the District of Columbia, or in restraint of trade or commerce between any such Territory and another, or between any such Territory or Territories and any State or States or the District of Columbia, or with foreign nations, or between the District of Columbia and any State or States or foreign nations, is hereby declared illegal. Every person who shall make any such contract or engage in any such combination or conspiracy, shall be deemed guilty of a misdemeanor, and, on conviction thereof, shall be punished by fine not exceeding five thousand dollars, or by imprisonment not exceeding one year, or by both said punishments, in the discretion of the court.

Sec. 4. The several circuit courts of the United States are hereby invested with jurisdiction to prevent and restrain violations of this act; and it shall be the duty of the several district attorneys of the United States, in their respective districts, under the direction of the Attorney-General, to institute proceedings in equity to prevent and restrain such violations. Such proceedings may be by way of petition setting forth the case and praying that such violation shall be enjoined or otherwise prohibited. When the parties

Section one declares illegal every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of interstate or foreign commerce; and provides a penalty. Section two is directed against monopolizing, or attempting to monopolize, any part of the trade or commerce among the several states, or with foreign nations; and provides a penalty. Section three declares illegal every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce *in* any Territory of the United States or *in* the District of Columbia, and likewise any such contract, etc., in restraint of trade or commerce between any two territories, or between any territory

complained of shall have been duly notified of such petition the court shall proceed, as soon as may be, to the hearing and determination of the case; and pending such petition and before final decree, the court may at any time make such temporary restraining order or prohibition as shall be deemed just in the premises.

Sec. 5. Whenever it shall appear to the court before which any proceeding under section four of this act may be pending, that the ends of justice require that other parties should be brought before the court, the court may cause them to be summoned, whether they reside in the district in which the court is held or not; and subpœnas to that end may be served in any district by the marshal thereof.

Sec. 6. Any property owned under any contract or by any combination, or pursuant to any conspiracy (and being the subject thereof) mentioned in section one of this act, and being in the course of transportation from one State to another, or to a foreign country, shall be forfeited to the United States, and may be seized and condemned by like proceedings as those provided by law for the forfeiture, seizure, and condemnation of property imported into the United States contrary to law.

Sec. 7. Any person who shall be injured in his business or property by any other person or corporation by reason of anything forbidden or declared to be unlawful by this act, may sue therefor in any circuit court of the United States in the district in which the defendant resides or is found, without respect to the amount in controversy, and shall recover three fold the damages by him sustained, and the costs of suit, including a reasonable attorney's fee.

Sec. 8. That the word "person," or "persons," wherever used in this act shall be deemed to include corporations and associations existing under or authorized by the laws of either of the United States, the laws of any of the Territories, the laws of any State, or the laws of any foreign country.

Approved, July 2, 1890.

26 Statutes at Large, pp. 209–210.

and the District of Columbia, or between either of these jurisdictions and any state or any foreign nation. The same penalty as in sections one and two is provided. Section four invests the circuit courts of the United States with jurisdiction to enforce the law, and provides that the federal government may institute proceedings in equity to prevent and restrain any violations thereof. Section five authorizes the courts to summon before them parties other than the defendants, if such seems to be necessary to effect justice. Section six authorizes the seizure and condemnation of property owned under any contract or by any combination, etc., prohibited in section one, and being transported in interstate or foreign commerce. Section seven confers upon persons injured by the violation of the law the right to sue the offending party for treble damages and the costs of the suit. Section eight provides that the word person as used in the act shall be deemed to include corporations and associations, no matter where incorporated.

For nearly a quarter of a century after 1890 the Sherman Act remained on the statute books unamended. Not until 1914 did Congress again give the subject of trust legislation the consideration that its importance demanded, and proceed to remedy the defects disclosed by experience and judicial interpretation. Such legislation dealing with trusts as was enacted in the meantime was mainly directed toward supplementing the Sherman Act in minor particulars.

The first addition to the Sherman Act came in 1894 as a part of the Wilson tariff bill, which became law on August 27, without receiving President Cleveland's signature. Section 73 of this law provided in substance that every combination, conspiracy, trust, agreement, or contract was illegal, when made by or between two or more persons or corporations, either of whom was engaged in importing any article into the United States, and when intended to operate in restraint of lawful trade, or free competition in lawful trade, or to increase the market price in the United States of any article imported into the United States, or of any manufacture into which such imported article entered.[1]

[1] 28 Statutes at Large, p. 570. Sections 74, 75, 76, and 77 of the Wilson

Provision was made for a penalty (fine, or fine and imprisonment) and for the seizure and condemnation of the property imported into the United States contrary to law.

Between 1894 and 1903 no further anti-trust legislation was enacted by the national government. The decision of the Supreme Court in the Knight case [1] in January, 1895, greatly limiting, as it then seemed, the effectiveness of the Sherman Act, might well have led to further legislation. But this decision not only limited the effectiveness of the Sherman Act, but seemed to call into question the very power of the federal government to deal effectively with trusts. Confronted with this decision President Cleveland, who viewed the organization of trusts with grave concern, turned to the states as best able to provide the necessary relief.[2] He might, to be sure, have recommended a constitutional amendment increasing the powers of the federal government, yet this suggestion would not have been acceptable to his party. Indeed it is not improbable that many members of his party actually welcomed the decision in the Knight case, since it seemed to bolster up the doctrine of state rights,—a doctrine dearer then than now to good Democrats. No matter how deeply concerned they might be over the establishment of trusts—the problem was by no means as serious at that time as it became shortly thereafter—one could hardly expect the members of the Democratic party in the middle nineties to support a constitutional amendment that would give to the federal government the power which, by the decision in the Knight case, it apparently lacked.

In 1897 the Republican party again returned to power. The platform of this party in 1896 had made no reference to trusts except a statement to the effect that the true American policy of protection is "equally opposed to foreign control and domestic monopoly;" [3] and one could thus perhaps hardly have looked for

tariff act were substantially identical with sections 4, 5, 6, and 7, respectively, of the Sherman Act of 1890.

[1] See p. 388.

[2] See Richardson, Messages and Papers of the Presidents, pp. 744–745.

[3] McKee, op. cit., p. 300.

any trust legislation from this party at that time. As a matter of fact the attention of the Republican party during President McKinley's first term was mainly directed toward tariff legislation, the war with Spain, and the currency situation.

Not until the closing years of the nineteenth century, however, did the trust problem reach a really acute stage. The organization of numerous trusts to cover fields formerly quite competitive created an entirely new situation. In the face of this situation President McKinley in December, 1899, in his annual message to Congress, took up the subject of trusts. He said in part: "Combinations of capital organized into trusts to control the conditions of trade among our citizens, to stifle competition, limit production, and determine the prices of products used and consumed by the people, are justly provoking public discussion, and should early claim the attention of Congress. . . . It is universally conceded that combinations which engross or control the market of any particular kind of merchandise or commodity necessary to the general community, by suppressing natural and ordinary competition, whereby prices are unduly enhanced to the general consumer, are obnoxious not only to the common law but also to the public welfare. . . . Whatever power the Congress possesses over this most important subject should be promptly ascertained and asserted." [1]

Early in 1900, also, the Industrial Commission, which had been appointed in 1898 to investigate trusts and monopolies, inter alia, made its preliminary report, recommending more detailed supervision over industrial corporations engaged in interstate operations. The testimony before this commission and the publication of its report focussed popular attention upon this subject. The state of the public mind at this time is indicated in the fact that the Republican party, which had hardly referred to trusts in its platform in 1896, inserted in its platform in 1900 this clause:

"We recognize the necessity and propriety of the honest cooperation of capital to meet new business conditions, and especially to extend our rapidly increasing foreign trade; but we condemn

[1] Cong. Record, December 5, 1899, p. 25.

all conspiracies and combinations intended to restrict business, to create monopolies, to limit production, or to control prices, and favor such legislation as will effectively restrain and prevent all such abuses, protect and promote competition, and secure the rights of producers, laborers, and all who are engaged in industry and commerce." [1]

Much more vigorous denunciation of trusts was made in the platform of the Democratic party, as is shown by the following extracts:

"Private monopolies are indefensible and intolerable. They destroy competition, control the price of all material and of the finished product, thus robbing both producer and consumer. They lessen the employment of labor and arbitrarily fix the terms and conditions thereof, and deprive individual energy and small capital of their opportunity for betterment. They are the most efficient means yet devised for appropriating the fruits of industry to the benefit of the few at the expense of the many, and unless their insatiate greed is checked, all wealth will be aggregated in a few hands and the republic destroyed.

"We pledge the Democratic party to an unceasing warfare in nation, state and city against private monopoly in every form.

"Tariff laws should be amended by putting the products of trusts upon the free list, to prevent monopoly under the plea of protection.

"We condemn the Dingley Tariff Law as a trust-breeding measure, skillfully devised to give the few favors which they do not deserve and to place upon the many burdens which they should not bear." [2]

To satisfy the popular demand for trust legislation, a number of bills were introduced in Congress in 1900. One of the principal legislative proposals was a constitutional amendment to give Congress adequate power to deal with trusts and to maintain an open field for competition in industry. This measure received a comfortable majority in the House, but failed to secure the two-thirds requisite for a constitutional amendment, and thus came

[1] McKee, op. cit., pp. 342–343.

[2] Ibid., pp. 334–336.

to naught.[1] Doubtless a partial explanation of the failure of this amendment is the fact that the decision of the Supreme Court in the Addyston Pipe case, rendered in December, 1899, had made it clear that the Sherman Act was more effective, and the power of the national government more extensive, than had theretofore been supposed.[2]

The constitutional amendment having failed of passage, the House immediately took up consideration of a bill to amend the Sherman Act. This bill was quite drastic, proposing among other things to deny the privilege of interstate transportation to manufacturing concerns organized for the purpose of monopolizing the manufacture or sale of articles of commerce, or of increasing or decreasing their price with the intent of preventing competition in their manufacture or sale.[3] In the opinion of the committee that reported out the bill the measure fully exhausted the power of Congress to control combinations and trusts by penal legislation. The bill was debated in the House during only one day, and after being amended so as to exclude labor organizations from its prohibitions was passed by the House by a vote of 274–1.[4] The sole dissenting vote was cast by Mr. James R. Mann, later the Republican leader of the House of Representatives. The Senate received the bill on June 4, referred it to the appropriate committee, and three days later adjourned sine die.

In 1903 two laws dealing with trusts were passed.[5] The first was an act to expedite the hearing and determination of cases arising under the anti-trust act and the act to regulate commerce.[6]

[1] Cong. Record, June 1, 1900, p. 6426; and House Report no. 1501, 56th Cong., 1st Sess.

[2] See p. 395.

[3] House Report no. 1506, 56th Cong., 1st Sess.

[4] Cong. Record, June 2, 1900, p. 6502.

[5] A proviso in the Legislative, Executive, and Judicial Appropriation Act of February 25, 1903, granted immunity to persons testifying in suits brought under the anti-trust or interstate commerce acts. 32 Statutes at Large, part I, p. 904. Because of the "immunity bath" decision (see p. 485) this immunity was limited in 1906 to natural persons only. 34 Statutes at Large, part I, p. 798.

[6] 32 Statutes at Large, part I, p. 823.

The purpose of this bill was to reduce the delay of the courts in settling important cases arising under the anti-trust and interstate commerce acts, and to that end it provided in substance that the circuit courts of the United States must give precedence to suits in equity arising under these acts, when the United States was a complainant, and when the Attorney General certified that the suits were of general public importance; and it further provided that appeals must be taken direct to the Supreme Court, and within sixty days from the entry of the decree of the lower court.

The second act established an agency to secure greater publicity of the affairs of industrial corporations. The organization of numerous trusts concerning which the public knew little had naturally created a popular demand for publicity. President Roosevelt in his first annual message to Congress had said "the first essential in determining how to deal with the great industrial combinations is knowledge of the facts—publicity." [1] In his second annual message he had repeated this recommendation, saying that "publicity can do no harm to the honest corporation; and we need not be overtender about sparing the dishonest corporation." [2] Congress yielded to his wishes in this matter (his wishes were those of the country), and in February, 1903, established, in the newly created Department of Commerce and Labor, a Bureau of Corporations, which, under the direction of the Secretary of Commerce and Labor, was to investigate the affairs of industrial corporations engaged in interstate or foreign commerce, the President of the United State to determine what part of the information thus obtained should be made public.[3] At the head of the Bureau there was to be a Commissioner of Corporations, appointed by the President, with a salary of $5,000. He was empowered to compel the attendance and testimony of witnesses, and the production of documentary evidence.

By the passage in 1903 of the act creating the Bureau of Cor-

[1] Cong. Record, December 3, 1901, p. 83.

[2] Ibid., December 2, 1902, p. 7.

[3] 32 Statutes at Large, part I, pp. 827–828.

porations, the Expedition Act, and the Elkins Act dealing with railroad rebates, the Republican party during President Roosevelt's first term made distinct progress in anti-trust legislation. But during President Roosevelt's second term, though he regularly referred to trusts in his messages to Congress, nothing whatever was accomplished.[1] Mention should be made, however, of one of his main recommendations. In his message of 1907 President Roosevelt had suggested that agreements among, or combinations of, corporations be submitted to a government body for its approval. In a special message presented to Congress on March 25, 1908, he took up this matter in more detail. He pointed out that in the modern industrial world combinations among business men and laboring men were absolutely necessary, and they were coming more and more to be necessary among farmers. The Sherman Anti-trust Law, though only partially effective against vicious combinations, had been construed so as to prohibit every combination for the transaction of modern business. He therefore recommended that some governmental authority, presumably the Commissioner of Corporations, be authorized to pass on the validity of contracts filed with it, and if within a definite time (say sixty days) the Commissioner had not prohibited such contract, it would not be deemed to be illegal unless in *unreasonable* restraint of trade.[2]

A bill embodying this suggestion was introduced in the Senate on April 1, 1908, only a week after the reading of the President's message. On January 26, 1969, the Committee on the Judiciary (to which the bill had been referred) brought out the measure, but with an adverse report. The committee in an unanimous report pointed out that the effect of the bill would be to confer a dispensing power, a power of granting immunity, on a mere bureau head (the Commissioner of Corporations for industrial corporations) or on an administrative body (the Interstate Commerce Commission for railroads), and in both instances without notice or hearing,—a course of procedure that

[1] Except for an amendment of the immunity provisions. See footnote to p. 326.

[2] Cong. Record, March 25, 1908, p. 3854.

would not be tolerated in any court in the country.[1] The Senate thereupon accepted the recommendation of the committee that the bill be postponed indefinitely.[2]

This bill was the only one proposing to amend the Sherman Act that was reported out of committee during the period intervening between the enactment of the 1903 legislation and the close of the Roosevelt administration in March, 1909. The only tangible evidence given by Congress of interest in trusts was in the passage of several resolutions of investigation. Among these were a joint resolution, approved by the President on March 7, 1906, instructing the Interstate Commerce Commission to make examinations into the subject of railroad discriminations and monopolies in coal and oil;[3] a resolution of the Senate directing the Attorney General to furnish it with a statement of all suits instituted by the Department of Justice under the Sherman Anti-trust Act and the Interstate Commerce Law, and the disposition made of the suits;[4] a resolution of the Senate directing the Secretary of Commerce and Labor to investigate the causes of the high price of lumber, and to determine whether there was a combination or trust in the supplying thereof;[5] and the passage by the House of a resolution to appoint a committee to investigate the paper industry, and to inquire whether there was a paper combination.[6]

William Howard Taft became President on March 4, 1909. President Taft made frequent reference to the trust question, and recommended far-reaching changes in our legislation. On January 7, 1910, in a special message to Congress on the anti-

[1] Senate Report no. 848, 60th Cong., 2nd Sess., p. 9.

[2] Cong. Record, January 26, 1909, p. 1395. Subsequently the Supreme Court of the United States in the Standard Oil and Tobacco cases in 1911 by the enunciation of its "rule of reason" made the passage of such a bill unnecessary; since these decisions, as will be pointed out later, limited the application of the Sherman Act to *unreasonable* contracts and combinations.

[3] Cong. Record, March 7, 1906, p. 3440.

[4] Ibid., June 25, 1906, p. 9089.

[5] Ibid., January 18, 1907, pp. 1330–1333.

[6] Ibid., April 21, 1908, p. 5033.

trust and interstate commerce laws, he expressed himself as hostile to trusts, and to all schemes to stifle competition and raise prices.[1] His main legislative recommendation was the enactment of a voluntary federal incorporation law, and provision by means of this law for the filing of reports with the Department of Commerce and Labor, and for the prevention of stock-watering and holding companies (except for special reasons approved by the proper federal authority). In subsequent messages he renewed his recommendation for a federal incorporation law, and recommended further that a Federal Corporation Commission, of the dignity and power of the Interstate Commerce Commission, be established to supervise the companies taking out federal charters; that the courts be empowered to invoke the aid of this body or the Commissioner of Corporations in drafting dissolution decrees; and that price cutting to eliminate competitors, exclusive contracts, and other kindred devices for stifling competition and effecting monopoly be specifically declared illegal and criminal.

Despite President Taft's great interest in anti-trust legislation, and the obvious need of action, only minor changes in the law dealing with trusts were made during his administration. On June 25, 1910, the Act to Expedite Hearings (1903) was amended. The act as amended provided that if a member of the circuit court was necessarily absent or disqualified, the justice of the Supreme Court assigned to that circuit (or the other circuit court judges) might designate some district judge within that circuit to sit in the court at the hearing of the suit.[2] It provided further that any case in which the judges were unable to agree on a decision or order, instead of being certified to the Supreme Court for review as if on appeal, should be retried before the court, reconstituted through the appointment by the Chief Justice of the Supreme Court of another circuit judge to sit with the court in the determination of that particular case.

In 1913 a bill was passed to provide for publicity in taking evidence under the Sherman Act. Senator Nelson, who re-

[1] Cong. Record, January 7, 1910, pp. 381 seq.

[2] 36 Statutes at Large, part I, p. 854.

ported the bill, explained that a suit had been instituted by the Department of Justice against the Shoe Machinery Trust, and that the federal judge had ordered the testimony before the master to be taken behind closed doors, instead of before the general public, as was the usual procedure.[1] The purpose of this bill, which was recommended by the Department of Justice, was to insure that testimony in cases under the anti-trust law be taken publicly as in open court. It was passed by the Senate on January 13; by the House on March 2; and signed by President Taft on March 3.[2]

The remaining legislation passed during the Taft administration was not particularly important. The practice of espionage on the business of competitors was dealt with by a clause in the Mann-Elkins Act of 1910, which provided that no carrier or its agent should disclose information concerning either the route, destination, or consignee of any shipment, when such information might be used to the detriment of the shipper, or improperly disclose his business transactions to a competitor.[3] The soliciting of such information was likewise made illegal. An act passed March 4, 1911, making an appropriation for the naval service for the fiscal year ending June 30, 1912, provided that "no part of this appropriation shall be expended for the purchase of armor or armament from any persons, firms or corporations, that have entered into any combination, agreement, conspiracy or understanding, the effect, object or purpose of which is to deprive the Government of fair, open and unrestricted competition in letting contracts for the furnishing of any of said armor or armament."[4] The act making appropriation for the fiscal year ending June 30, 1913 (passed August 22, 1912), contained a similar provision, somewhat modified in its phraseology, which applied not only to armor and armament, but also to structural steel, ship plates, and machinery.[5]

[1] Cong. Record, January 13, 1913, p. 1434.
[2] 37 Statutes at Large, part I, p. 731.
[3] 36 Statutes at Large, part I, p. 553.
[4] Ibid., p. 1288.
[5] 37 Statutes at Large, part I, p. 355.

The act providing for the opening and operation of the Panama Canal, passed August 24, 1912, contained a clause forbidding the use of the canal to any ship owned, chartered, operated, or controlled by any person or company that was doing business in violation of the Sherman Act of 1890, or sections seventy-three to seventy-seven of the Wilson Tariff Act of 1894, or any act amending or supplementing either of these.[1] The question of fact was to be determined by the courts upon the institution of suit by the shipper or the Attorney General against the owners or operators of the ship. In 1913 also (by the passage of H. R. 25002) sections 73 and 76 of the Wilson Tariff Act of 1894 were modified slightly.[2]

In addition to these bills, a number of resolutions were adopted. Among them were: a House resolution requesting the President to furnish it with information concerning a combination between the United States Steel Corporation and its subsidiary companies; [3] a House resolution appointing a committee (Mr. Hardwick, chairman) to investigate the American Sugar Refining Company; [4] a House resolution appointing a committee (Mr. Stanley, chairman) to investigate the United States Steel Corporation; [5] a Senate resolution appointing a committee (Mr. Clapp, chairman) to report desirable changes in the laws controlling corporations engaged in interstate commerce; [6] a House resolution to investigate the money trust (Mr. Pujo chairman); [7] and a House resolution directing the Attorney General to inform it whether there was a smelter trust in the United States, including the American Smelting and Refining Company.[8]

[1] 37 Statutes at Large, part I, p. 567.
[2] See 37 Statutes at Large, part I, p. 667.
[3] Cong. Record, June 16, 1910, p. 8249.
[4] Ibid., May 9 1911, p. 1147.
[5] Ibid., May 16, 1911, p. 1234.
[6] Ibid., July 26, 1911, p. 3226.
[7] Ibid., February 24, 1912, p. 2419.
[8] Ibid., March 12, 1912, p. 3200.

CHAPTER XV

THE TRUST LEGISLATION OF 1914[1]

LEGISLATIVE HISTORY

As the end of President Taft's administration drew near it became clear that no important trust legislation would be enacted. The Democratic party in the summer of 1912 nominated Woodrow Wilson as its candidate for the presidency, and adopted a platform promising warfare on industrial monopoly. The platform repeated the old battle cry, "a private monopoly is indefensible and intolerable," and demanded the enactment of such additional legislation as might be necessary to make it impossible for a private monopoly to exist in the United States.[2] Legislation to prevent holding companies, interlocking directorates, price discrimination, and stock-watering was urged. Regret was expressed that the Sherman Act through judicial construction had lost much of its efficacy, and legislation to restore its effectiveness was recommended. Finally, the declaration was made that articles produced by trusts should be placed upon the free list.

The Republican platform affirmed the opposition of the Republican party to special privilege and monopoly; congratulated the party upon the passage of the Sherman Act, and its successful enforcement; and asserted that the party would take no back-

[1] On the trust legislation of 1914 see: Congressional Record; Commercial and Financial Chronicle; Durand, The Trust Problem, ch. 5; Young, The Sherman Act and the New Anti-Trust Legislation, Journal of Political Economy, 23, pp. 201–220, 305–326, and 417–436; Stevens, American Economic Review, 4, pp. 840–855, and 5, pp. 38–54; Seager, Political Science Quarterly, 30, pp. 448–462; Montague, The Federal Trade Commission and the Clayton Act, in Stetson, Some Legal Phases of Corporate Financing, Reorganization and Regulation, pp. 275–326; House Report no. 627, 63rd Cong., 2nd Sess.; Senate Report no. 698, 63rd Cong., 2nd Sess.

[2] Campaign Text Book of Democratic Party, 1912, pp. 2, 6.

ward step to permit the reëstablishment of intolerable conditions.[1] It advocated the enactment of supplementary legislation defining as criminal those specific acts that uniformly characterized attempts to restrain and monopolize trade, to the end that those who desired to obey the law might have a guide for their action, and that those who intended to violate it might not escape punishment. Finally, it suggested the creation of a federal trade commission, which would perform many of the functions then exercised by the courts.

More vigorous in tone was the platform of the newly created Progressive party. The trust plank of this platform, representing the views of the leader of the party, urged the creation of a federal administrative commission to exercise somewhat the same degree of control over trusts that the Interstate Commerce Commission exercised over interstate railways.[2] This commission, it became apparent from Mr. Roosevelt's utterances, was to regulate trusts—whenever competition could not be restored—and to fix the prices of the articles produced by them, when necessary.[3] Mr. Roosevelt favored, it is true, the enactment of additional legislation to prohibit certain unfair trade practices, such as local price discrimination and rebates, the elimination of which, he held, would lead to the restoration of competition in some instances; but he differed fundamentally from the Democratic and Republican candidates in proposing to recognize *some* trusts as a natural evolution instead of as a fraud on the body politic.

In the election campaign of the fall of 1912 the trust question played an important part. Probably the tariff and the trusts received greater attention than any other issues. But we may not conclude that the stand of the respective candidates on these issues determined the outcome of the campaign. Whatever the issues President Taft was certain to be defeated.

[1] Republican Campaign Text Book, 1912, pp. 272–273.

[2] The platform may be found in Roosevelt, Progressive Principles, edited by E. H. Youngman, pp. 314–330. See especially p. 318.

[3] See Outlook, 99, p. 655 (November 18, 1911); and 102, pp. 105–106 (September 21, 1912).

His party had failed to keep its promise to revise the tariff downward, and the acquiescence of the President in this failure turned the people against him. Already in 1910 the capture of the House by the Democrats attested the failure of his administration. When there was added to this state of affairs the action of the Old Guard in defeating the will of the Republicans (as expressed in numerous primaries), by the nomination of Mr. Taft as their candidate, his defeat was made certain. Theodore Roosevelt, who by the action of the people in the primaries was entitled to the Republican nomination, at once organized the Progressive party,—a party which developed a considerable strength because of the popularity of its leader, the program of social justice for which it stood, and no doubt because of a feeling that Mr. Roosevelt had been the victim of a fraud. But the result of the election was never in doubt. Woodrow Wilson conducted a dignified campaign, in which personalities were not indulged in, confined himself largely to a few issues in which the preceding administration had made a signal failure, and received an enormous majority of the electoral votes.

During the course of the campaign Mr. Wilson had promised further anti-trust legislation. As he had said, "I take my stand absolutely, where every progressive ought to take his stand, on the proposition that private monopoly is indefensible and intolerable." [1] The enactment of anti-trust legislation, however, was to wait upon the completion of two other programs,—tariff reform and banking reform. The Congress which was called in special session on April 7, 1913, passed the Simmons-Underwood tariff bill on October 3, 1913—a measure which, in view of the Democratic doctrine that the trusts have been promoted by the tariff, may be regarded as a partial remedy for the trusts—and passed the Federal Reserve Act on December 23, 1913. The decks were now cleared for trust measures.

The message of the President on trust legislation was delivered to Congress in person on January 20, 1914.[2] His trust pro-

[1] Wilson, New Freedom, p. 172.

[2] Cong. Record, January 20, 1914, pp. 1962–64.

gram was founded on the conviction that "private monopoly is indefensible and intolerable,"—a proposition which he held all were agreed upon. He said that we propose to be the spokesmen of the best informed men of the business world, who condemn the methods and processes and consequences of monopoly as we condemn them. His program was to be a comprehensive one, but not radical or unacceptable. There was to be "nothing essential disturbed, nothing torn up by the roots, no parts rent asunder which can be left in wholesome combination." The object, he said, was not to unsettle business, but to pass laws to be the bulwarks and safeguards of industry against the forces that had disturbed it. The items in this program were: first, laws that would effectually prevent such interlockings of the personnel of the directorates of great corporations as resulted in making those who affected to compete in fact partners and masters of some whole field of business. Such a prohibition, he said, would bring new men, new energies, a new spirit of initiative, and new blood into the management of our great business enterprises; it would open the field of industrial development and origination to scores of men who had been obliged to serve when their abilities entitled them to direct. Second, a law that would confer upon the Interstate Commerce Commission the power to superintend and regulate the financial operations by which the railroads were henceforth to be supplied with the money they needed for their proper development. Such a law was to be one step toward the necessary separation of the business of production from the business of transportation. Third, an explicit legislative definition of the policy and meaning of the existing anti-trust law, a prohibition item by item of the practices of monopoly which experience had disclosed, in order that there need be no risk of falling under the condemnation of the law from an inability to find out just what the law was. Fourth, the creation of an interstate trade commission. This body would not be empowered to make terms with monopoly or to assume control of business; rather it was to serve as an instrument of information and publicity, and to assist in the dissolution of concerns which had combined to a degree inconsistent

with the public interest and the freedom of trade. Fifth, the establishment of the principle that penalties and punishments should fall not upon business itself, to its confusion and interruption, but upon the individuals who used the instrumentalities of business to do things which public policy and sound business practice condemned. Every act of business is done at the command or upon the initiative of some ascertainable person or group of persons; and these should be held individually responsible and the punishment should fall upon them, not upon the business organization of which they made illegal use. Sixth, the prohibition of holding companies. The President presented to Congress for its consideration the question whether we should require individuals owning stock in several companies which ought to be independent, but which on account of common stock ownership were brought under a common control, to decide in which of them they would elect the right to vote. Seventh, relief for the individuals who had been injured by the many dislodging and exterminating forces of combination. Private individuals who claim to have been injured by these processes should be given the right, he held, to found their suits for redress upon the facts and judgments proved and entered in suits by the government when the government had upon its initiative sued the combinations complained of and won its suit. It was not fair, he said, that the private litigant should be obliged to establish again the facts which the government had already proved.

Immediately upon the conclusion of the President's address the House voted to refer that part of the message which related to a Trade Commission and to the regulation of railway securities to the Committee on Interstate and Foreign Commerce, and the balance to the Committee on the Judiciary.[1] Two days later it was publicly announced that the trust legislation would be embodied in five separate bills: (1) a Trade Commission bill; (2) an Interlocking Directorates bill; (3) a Definitions bill; (4) a Trades Relations bill, dealing with unfair competition; and (5) a Railroad Securities bill.[2] Shortly after these bills had been made

[1] Cong. Record, January 20, 1914, p. 1980.

[2] Chron., 98, p. 273 (January 24, 1914).

public, hearings upon them began. Later the five bills were consolidated into three: (1) the Trade Commission bill; (2) the Clayton bill, which included the Interlocking Directorates bill and the Trade Relations bill (the Definitions bill was dropped); and (3) the Railroad Securities bill. This third measure, which was to give the Interstate Commerce Commission authority to regulate the issues of securities by common carriers and to deal with interlocking directorates among common carriers, was designed to prevent the occurrence in the future of such scandals as the Rock Island and New Haven episodes. The bill was passed by the House on June 5 by a vote of 325–12,[1] but early in September the announcement was made that, in view of the disturbed conditions created by the European War, the President had consented to the postponement of the measure. Thus was another illustration given of the baneful effect of war on domestic policies.

Before analyzing in some detail the two trust bills that were enacted into law, we may outline briefly their legislative history. The first—the Trade Commission bill (H. R. 12120)—was introduced in the House on January 22 by Representative Clayton, and referred by the House to the Committee on Interstate Commerce.[2] At the same time this bill was introduced in the Senate as S. 4160. During the course of the committee hearings it became apparent that the bill did not fully carry out the ideas of the President, and therefore Chairman Adamson on February 16 appointed a sub-committee, of which Representative Covington of Maryland was made chairman, to draft a new bill.[3] On March 14 Mr. Covington introduced in the House a new bill (H. R. 14631), which represented the unanimous views of the sub-committee.[4] This bill was referred to the Committee on Interstate Commerce. One month later (April 13) a new bill (H. R. 15613), a revised draft of the former bill, was introduced by Representative Covington, and referred by the House to the

[1] Cong. Record, June 5, 1914, p. 9912.
[2] Ibid., January 22, 1914, pp. 2142, 2150–1.
[3] Chron., 98, p. 567 (February 21, 1914).
[4] Cong. Record, March 14, 1914, p. 4886.

Committee on Interstate Commerce.[1] The next day this committee reported the bill to the House without amendment, accompanied by a report (no. 533).[2] The committee in its report stated that the bill provided for a trade commission in accordance with the views of the President as expressed in his message to Congress. The bill was framed on the principle of preserving competitive conditions in interstate commerce; the commission had not been given power to make terms with monopoly, to regulate prices or production, to declare any particular corporation or agreement innocuous, or to issue orders. The report was concurred in by all the Democratic members of the committee except two who did not believe the bill was sufficiently drastic, and by all the Republican members of the committee; in fact the preparation of the bill and its course through Congress were marked by a comparative absence of political considerations, the Republicans coöperating with the Democrats to effect its passage. In part this fortunate state of affairs was due to the widespread demand for the establishment of a commission—the poll conducted by the Chamber of Commerce of the United States was eloquent testimony as to the strength of this demand—and in part it was due to the skill and courtesy of Representative Covington, who carefully avoided stirring up antagonisms or factional differences. On May 19 debate on the bill began in the House. Amended in only one particular (and that a minor one), the bill passed the House on June 5, 1914.[3] The vote on the measure was not recorded, but that the opposition to its passage was slight is attested by the fact that a motion to recommit the bill, offered by Representative Murdock of Kansas (a Progressive), was defeated by a vote of 151 to 19.[4] (Not all of the nineteen, however, were to be regarded as hostile to the measure, for Mr. Murdock himself stated that he was not opposed to the passage of the bill.) The House bill was referred by the Senate to the Committee on Interstate Commerce; and on June 13 was reported from the

[1] Cong. Record, April 13, 1914, p. 6648.
[2] Ibid., April 14, 1914, p. 6714.
[3] Ibid., June 5, 1914, p. 9910.
[4] Ibid.

committee. The action of the committee consisted in striking out all of the House bill except the enacting clause, and substituting therefor the provisions of the Senate bill (S. 4160), with the addition of several sections dealing with unfair competition and foreign trade practices. On June 25 the Senate took up the consideration of this bill. Debate upon it occupied a large share of the Senate's attention during the month that followed, the principal bone of contention being the unfair competition provisions which had been added to the bill by the Senate Committee. On July 22 the Democratic members of the Senate at a caucus agreed that the bill should be kept constantly before the Senate until its final disposition.[1] Finally on August 4 a unanimous consent agreement was entered into that the Senate would vote on the bill not later than August 5.[2] On that day the bill, amended in many particulars, passed the Senate by a vote of 53 to 16, 27 not voting.[3] Only two Democrats voted against the bill (though quite a number were absent) and twelve Republicans voted for it.

The House disagreeing to the amendments of the Senate, a conference became necessary. The conference committee labored over the bill for nearly a month, endeavoring to agree upon a measure that would include the fundamental provisions of both bills. On September 4 the result of their labors was presented to the Senate and to the House. The conference report was agreed to in the Senate on September 8 by a vote of 43–5,[4] the main features of the debate being the exceeding difficulty experienced in maintaining a quorum. The conference report was taken up in the House on the 10th. Representative Mann of Illinois, the leader of the opposition, expressed the prevailing sentiment when he said that the discussion on the bill had been devoid of partisan politics from the start, and that it was a good bill.[5] The House on the 10th agreed to the conference re-

[1] Chron., 99, p. 238 (July 25, 1914).
[2] Cong. Record, August 4, 1914, p. 13235.
[3] Ibid., August 5, 1914, p. 13319.
[4] Ibid., September 8, 1914, p. 14802.
[5] Ibid., September 10, 1914, p. 14940.

port.[1] Nothing now remained but the signature of the President; and this was affixed on September 26, 1914.

The second of the trust measures—the Clayton bill (H. R. 15657)—was introduced in the House on April 14.[2] Of the three tentative bills before the Committee on the Judiciary one (the Definitions bill) had been dropped, and the other two had been consolidated. A Definitions bill had been urged by President Wilson in his message to Congress, but the objection was raised that a specific enumeration of offenses under the act might limit the scope of the anti-trust acts. The Attorney General, for example, expressed the opinion that a legislative definition of offenses might weaken the act. Moreover, it was certain that it would be years before the various offenses defined in the bill would receive judicial interpretation. Apparently the President became convinced of the force of these objections; and as a result the Definitions bill was dropped. The remaining bills (the Interlocking Directorates bill and the Trade Relations bill), with some new matter, were consolidated into one,—the Clayton bill. As one commentator has put it, two separate measures were better targets for criticism than a single bill, and at the same time they did not afford as good a rallying-ground for those who were willing to support the administration.[3] The Clayton bill was referred by the House to the Committee on the Judiciary. On May 6 the bill was reported from the committee with an amendment, accompanied by a report (no. 627).[4] Debate on the bill began on May 22. It occupied the attention of the House until June 5, when it was passed with its amendments by a vote of 277 to 54.[5] Only one Democrat voted against it, while forty-three Republicans and sixteen Progressives voted for it.[6] In spite of the charge made against the bill that it was conceived in a spirit of partisanship in marked contrast to the Trade Commis-

[1] Cong. Record, September 10, 1914, p. 14933.
[2] Ibid., April 14, 1914, p. 6714.
[3] Young, Journal of Political Economy, 23, p. 320.
[4] Cong. Record, May 6, 1914, p. 8201.
[5] Ibid., June 5, 1914, p. 9911.
[6] Chron., 98, p. 1814 (June 13, 1914).

sion bill, it received the support of a large number of Republicans and Progressives.

The Clayton bill was presented to the Senate, and on June 6 referred to the Committee on the Judiciary.[1] On the 22nd of July it was reported out with amendments and with a report (no. 698).[2] Consideration of the bill by the Senate in Committee of the Whole was begun on August 11; and for the next three weeks the Senate concentrated its attention upon it. On September 2 the measure, amended in many vital particulars, passed the Senate by a vote of 46–16.[3] The forty-six votes for the measure were cast by thirty-eight Democrats, seven Republicans, and one Progressive. The sixteen votes in opposition were all cast by Republicans.

The amendments to the House bill made by the Senate were numerous and far-reaching, and a conference was therefore necessary. The report of the conference committee was presented to the Senate on September 23, read on September 26, and taken up for debate on September 28. Vigorous objection to the report was made, particularly by Senator Reed of Missouri, who held that the teeth had been removed from the bill, his principal objection being the failure of the conferees to retain the criminal penalties provided for by the House. In order to effect the restoration of the criminal penalties, he made a motion on October 5 to recommit the bill to conference. This was defeated by a vote of 35–25.[4] The Senate thereupon by a vote of 35–24 agreed to the conference report.[5] On October 7 the report was taken up in the House, and the next day the report was agreed to by a vote of 245–52.[6] The signature of the President was affixed on October 15, 1914, thus bringing to a conclusion the anti-trust legislation of the year.

THE TRADE COMMISSION ACT

In describing the provisions of the Trade Commission Act we shall take up, first, the organization of the Commission;

[1] Cong. Record, June 6, 1914, p. 9929.
[2] Ibid., July 22, 1914, p. 12468.
[3] Ibid., September 2, 1914, p. 14610.
[4] Ibid., October 5, 1914, p. 16170.
[5] Ibid.
[6] Ibid., October 8, 1914, p. 16344.

second, its principal powers and duties; and third, some miscellaneous provisions.

Organization of the Commission

The act provided for the creation of a Federal Trade Commission of five members to be appointed by the President, with the advice and consent of the Senate. The salary of each member was fixed at $10,000 a year; and the term of office at seven years, except for the first appointees, who were to serve for three, four, five, six, and seven years, and except for appointments to fill vacancies, in which case the unexpired term was to be filled out. Not more than three of the five commissioners might be of the same political party. No commissioner might engage in any other business, vocation, or employment. The commissioners might be removed by the President for inefficiency, neglect of duty, or malfeasance in office.

Upon the organization of the Commission and the election of its chairman, the Bureau of Corporations and the offices of the Commissioner and Deputy Commissioner of Corporations were to cease to exist; but the Commission was to continue all the pending investigations and proceedings of the Bureau, to retain all the clerks and employees of the Bureau at their former grades and salaries, and to take possession of all the records, papers, and property of the Bureau, including any unexpended funds.

The Commission was to appoint a secretary at a salary of $5,000 a year, and to have authority to employ and fix the compensation of such attorneys, special experts, examiners, clerks, and other employees as it might from time to time find necessary, and for whom Congress might from time to time make appropriation. With the exception of the secretary, a clerk to each commissioner, the attorneys, and the special experts and examiners, all employees of the commission were to be a part of the classified civil service.

Powers and Duties of the Commission

The principal powers of the Commission may be classified

under two heads: I. Investigation; II. The prevention of unfair methods of competition in commerce.[1]

I. The powers of investigation possessed by the Commission are primarily those that relate: (A), to all corporations engaged in commerce, other than banks and common carriers; and (B), to all corporations guilty or alleged to be guilty of violating the anti-trust laws. The first set of powers obviously relates to a larger number of corporations; but the second set relates to a greater variety, for it includes not only industrial corporations, but also banks and common carriers, which as to their ordinary operations are under the control of other government bodies.

A. The powers of investigation that relate to those corporations engaged in commerce which are within the especial jurisdiction of the Commission (industrial corporations) are:

(1) "To gather and compile information concerning, and to investigate from time to time the organization, business, conduct, practices, and management of any corporation engaged in commerce, excepting banks and common carriers subject to the Act to regulate commerce, and its relation to other corporations and to individuals, associations, and partnerships."[2] This power is only a little broader than that possessed by the Bureau of Corporations. The main differences are that the Bureau of Corporations in its investigations was subject to the direction and control of the Secretary of Commerce and Labor, whereas the Federal Trade Commission is not; that the Bureau was not specifically authorized to investigate "business" and "practices," as well as organization, conduct, and management; and that the authority of the Bureau included banks, while that of the Commission does not.

(2) To require, by general or special orders, the corporations subject to its especial control to file with it "in such form as the

[1] The term commerce as defined in the act means "commerce among the several States or with foreign nations, or in any Territory of the United States or in the District of Columbia, or between any such Territory and another, or between any such Territory and any State or foreign nation, or between the District of Columbia and any State or Territory or foreign nation."

[2] Section six (a).

commission may prescribe" annual or special reports, or answers in writing to specific questions, furnishing to the Commission such information as it may require regarding their organization, business, conduct, practices, management, and their relation to other corporations, partnerships, and individuals. These reports and answers are to be made under oath, or otherwise, as the Commission may prescribe, and to be filed within such reasonable period as the Commission may set.[1] Any corporation which fails to file the annual or special report within the time fixed by the Commission is subject to a penalty of $100 per day, to be recovered by the Department of Justice, and paid into the Treasury of the United States.[2] Moreover, any person who willfully makes, or causes to be made, any false entry or statement of fact in any report made to the Commission, or who willfully makes any false entry in any account, record, or memorandum kept by any corporation subject to this act, or who willfully neglects to make full and correct entries in such accounts, etc., of all transactions pertaining to the business of the corporation, or who willfully removes out of the jurisdiction of the United States, or willfully alters or by any means falsifies, any documentary evidence of such corporation, is subject to a fine of not less than $1,000 nor more than $5,000, or to imprisonment for a term not to exceed three years, or to both such fine and imprisonment.[3] The House and the Senate bills had provided that the Commission might prescribe "as near as may be a uniform system of annual reports." This was modified to read that these reports, including the special reports, should be made "in such form as the commission may prescribe." In giving the Commission power to call for annual and special reports the Trade Commission Act represents a distinct advance over the act creating the Bureau of Corporations. In the latter act there was no compulsory power provided whereby the Bureau could obtain regular reports, even assuming, what is unlikely, that the

[1] Section six (b).

[2] Section ten. The penalty does not lie until thirty days after the date set by the Commission.

[3] Section ten.

general powers of investigation conferred on the Bureau included the power to call for reports. But in the Trade Commission Act the power is specifically given, and a penalty is provided.

(3) The Commission has power to classify corporations from time to time, and to make rules and regulations for the purpose of carrying out the provisions of the act.[1] It is not clear just what the significance of this clause is. Mr. Stevens holds that the effect of this provision combined with the power to call for reports is apparently to give the Commission the power in its discretion to make a classification of corporations, and then, if the Commission deems it fitting, to prescribe a uniform system of accounting for the reports of all members of each class.[2] However, neither the Commission nor the courts have as yet passed upon the meaning of this subsection.

B. We come now to those powers of investigation that relate to corporations guilty or alleged to be guilty of violating the anti-trust laws. To some extent the powers to be now considered are broader than those of mere investigation, but they may be included here, since they embrace in every instance thorough investigation. The Commission has the following powers:

(4) "Upon the direction of the President or either House of Congress to investigate and report the facts relating to any alleged violations of the antitrust Acts by any corporation."[3] In the House and Senate bills the Commission was made subject in this matter to the direction of the Attorney General also, but in view of the fact that the Attorney General was the head of an executive department, it was concluded that the direction of the President would be sufficient. Accordingly this provision was eliminated in conference. It is expected that the effect of this clause will be to transfer to the Commission much of the work of investigation formerly carried on by the Department of Justice.

(5) "Upon the application of the Attorney General to investigate and make recommendations for the readjustment of

[1] Section six (g).

[2] Stevens, American Economic Review, 4, pp. 849–850.

[3] Section six (d).

the business of any corporation alleged to be violating the anti-trust Acts in order that the corporation may thereafter maintain its organization, management, and conduct of business in accordance with law." [1] It will be noticed that the Commission exercises this power only upon the application of the Attorney General, and that the Attorney General is under no compulsion to accept the recommendations of the Commission. Should there be coöperation between these two bodies—as Congress doubtless intended—this provision will prove helpful.[2] The increasing activity of the Department of Justice in recent years has engendered in a number of concerns the desire to readjust their business in such a way as to avoid a government suit. Having proven unsuccessful in securing the establishment of a Commission with power to give them an "immunity bath," i. e., to pass on the reasonableness of their agreements, these concerns desire an assurance that they will not be prosecuted by the Attorney General then in office. This assurance they can now obtain by a readjustment of their affairs in a manner approved by the Department of Justice. It is highly desirable that these voluntary reorganizations be promoted, as they effect the desired end without the delay and expense of court proceedings. And it was the opinion of Congress that the Commission was better constituted than the Department of Justice to suggest a satisfactory *economic* reorganization, leaving to the Department the acceptance of the plan as being *legally* satisfactory.

(6) Upon the request of the court, and as a master in chancery, to ascertain and report an appropriate form of decree in any suit in equity brought under the direction of the Attorney General as provided in the anti-trust acts.[3] The court may adopt or reject the report in whole or in part, and may enter such de-

[1] Section six (e).

[2] Down to May, 1920, the Attorney General had called upon the Commission for recommendations only twice: once in the case of certain news print manufacturers, and once in the case of the California Raisin Association. Correspondence with Federal Trade Commission.

[3] Section seven.

cree as it judges proper. This provision, should the courts take advantage of it, will prove distinctly helpful. The formulation of a decree, particularly a dissolution decree, is an exceedingly difficult matter,—one calling for skill, judgment, and detailed technical knowledge of the industry involved. The exigencies of the situation may require that the trust be split up into a number of separate units. These units must not be so large as to make competition between them unlikely; nor must they be so small as to sacrifice efficiency. The problem is thus primarily economic, rather than legal, and the provision for the preparation of a decree by the Trade Commission is an indication that Congress recognized this to be the case.[1] 'Should the courts invoke the aid of the Commission, it is unlikely that dissolution decrees as ineffective as those in the oil and tobacco cases will be again entered. It is true that the Attorney General invoked the aid of the Bureau of Corporations in the dissolution of the tobacco trust, and that the principal expert of the Bureau reported that the distribution of business under the plan was economically satisfactory.[2] Yet there is considerable difference between an official of the Bureau acting extra-officially and five Trade Commissioners performing a service specifically provided for in the law, in order that earlier farces may not be repeated. However, to date [3] the courts have not availed themselves of the benefits of this section.

(7) "Whenever a final decree has been entered against any defendant corporation in any suit brought by the United States to prevent and restrain any violation of the anti-trust Acts, to make investigation, upon its own initiative, of the manner in which the decree has been or is being carried out, and upon the

[1] Attorney General Wickersham in his Annual Report for 1911 (p. 6) stated that the problems involved in working out the tobacco dissolution plan were economic rather than legal, and admitted that neither the courts nor the Department of Justice were properly equipped to work out such problems, save in exceptional cases.

[2] Annual Report of the Attorney General, 1911, p. 7.

[3] May, 1920. In the glucose case a lower court requested the Commission to prepare a dissolution decree; but the case was appealed, and the Commission did not actually prepare a decree.

application of the Attorney General it shall be its duty to make such investigation. It shall transmit to the Attorney General a report embodying its findings and recommendations as a result of any such investigation, and the report shall be made public in the discretion of the commission." [1] This provision was taken from the House bill, except that in that bill the Commission was required to investigate on its own initiative into the observance of the decree, whereas in the act the Commission is required to investigate only upon the request of the Attorney General. This function is one that was formerly exercised by the Department of Justice, but especial legislative provision for its exercise by the Commission either on its own initiative or upon the initiative of the Department of Justice will doubtless cause it to be performed more regularly and conscientiously.

(8) "To investigate, from time to time, trade conditions in and with foreign countries where associations, combinations, or practices of manufacturers, merchants, or traders, or other conditions, may affect the foreign trade of the United States, and to report to Congress thereon, with such recommendations as it deems advisable." [2]

(9) To make public from time to time such portions of the information obtained by it, except trade secrets and the names of customers, as it shall deem expedient in the public interest; and to make annual and special reports to Congress, and to submit therewith recommendations for additional legislation; and to provide for the publication of its reports and decisions.[3] The ability of the Commission to determine for itself what information it shall make public, rather than have the matter determined by the President, gives it added prestige. It is to be hoped that the Commission will make public all the information it secures that bears on the trust question. The trusts can no longer plead the sacro-sanct character of their business;

[1] Section six (c).

[2] Section six (h). Acting under the authority granted by this section the Commission undertook and has completed (1916) an investigation of Cooperation in American Export Trade.

[3] Section six (f).

this business has reached such dimensions as to cause them to be imbued with a public interest. If they are not public service corporations, as that phrase is technically used, neither are they private institutions. The annual reports to Congress making recommendations for additional legislation will undoubtedly influence the future course of trust legislation, just as the recommendations of the Interstate Commerce Commission have influenced the trend of railway legislation. No doubt the experience of the Interstate Commerce Commission with the railways made Congress surer of its ground in the creation of a Trade Commission, yet that experience afforded no complete parallel. The Trade Commission deals with a much larger number of corporations, pursuing diverse businesses; and it is established to restore and preserve competitive conditions rather than to fix the charges for service performed by corporations that are generally recognized as natural monopolies. Under these circumstances it is undoubtedly better that the country should proceed surely, even if it seems to be proceeding slowly; for if progress is sure, the goal is likely to be sooner attained.

II. In addition to its powers of investigation, the Commission has power over unfair methods of competition.[1] Section five declares that "unfair methods of competition in commerce are hereby declared unlawful."[2] The Commission is then directed to prevent persons, partnerships, or corporations (except banks, and common carriers subject to the acts to regulate commerce) from using unfair methods of competition in commerce. The remaining provisions of this section, dealing largely with procedure, may be enumerated seriatim. (1) If the Commission has reason to believe that any person, partnership, or corporation (save those excepted above) has been or is using any unfair method of competition in commerce, and if it shall appear to the Commission that a proceeding by it would be in the interest of the public, it shall serve upon such person, firm, or corporation a complaint stating its charges, and containing a notice of a

[1] For a definition of commerce as used in the act see p. 344.

[2] On the subject of unfair competition, see the report of the Bureau of Corporations on Trust Laws and Unfair Competition.

hearing to be held at least thirty days after the service of the complaint. (2) The party complained of shall have the right to appear at the time fixed and show cause why an order should not be entered requiring it to desist from the violation of the law as charged in the complaint. (3) Other parties may be allowed by the Commission to intervene and appear in the proceedings by counsel or in person. (4) If upon such hearing the Commission shall be of the opinion that the method of competition in question is prohibited by the act, it shall make a written report in which it shall state its findings as to the facts, and it shall order such corporation to desist from using such method of competition. (5) If the order is not obeyed, the Commission may apply to the circuit court of appeals of the United States, within any circuit where the method of competition in question was used or where such corporation carries on business, for the enforcement of its order. (6) Upon the filing of the application and of the transcript of record, the court shall have jurisdiction of the proceeding, and shall have power to make an order affirming, modifying, or setting aside the order of the Commission. (7) The findings of the Commission as to the facts, if supported by testimony, shall be conclusive. (8) If either party shall apply to the court for leave to adduce additional evidence, and shall show to the satisfaction of the court that such additional evidence is material and that there were reasonable grounds for the failure to adduce such evidence in the proceeding before the Commission, the court may order such additional evidence to be taken before the Commission. (9) By reason of the additional evidence, the Commission may modify its findings as to the facts, or make new findings, which findings, if supported by testimony, shall be conclusive; and the Commission shall file its findings and its recommendation, if any, for the modification or setting aside of its original order. (10) The judgment and decree of the court shall be final, except that an appeal may be taken to the Supreme Court upon certiorari as provided in section two hundred and forty of the Judicial Code. (11) Any party required by an order of the Commission to desist from using an unfair method of competition may obtain a re-

view of this order in the aforesaid circuit court of appeals by filing a written petition asking that the order of the Commission be set aside. (By this provision the party complained of need not wait for the Commission to act; it can proceed upon its own account to test the validity of the Commission's order.) (12) The Commission upon being served with a copy of this petition shall file in the court a transcript of the record as above provided. (13) Upon the filing of the transcript the court shall have the same jurisdiction of the proceeding as in the event of an application by the Commission for the enforcement of its order. (14) The jurisdiction of the circuit court of appeals of the United States to enforce, set aside, or modify orders of the Commission shall be exclusive. (This is true whether the initiative in bringing the order of the Commission into court be taken by the Commission or by the party complained of.) (15) The proceedings in the circuit court of appeals shall be given precedence over all other cases pending therein, and shall be in every way expedited. (16) No order of the Commission or judgment of the Court to enforce the same shall in any wise relieve or absolve any person, partnership, or corporation from any liability under the anti-trust acts.

The Senate bill had declared unlawful "unfair competition." The objection had been raised in the course of the debate in the Senate that the term was too vague; that business men would not know what in law was "fair" and what was "unfair." Even Representative Covington stated that when the proposition to prohibit "unfair competition" was first mooted in the House he believed that the phrase was too vague to be enforced.[1] But further reflection and study convinced him as well as most of the other doubters that the phrase had a definite significance in the decisions of the courts;[2] and the bill passed the Senate in this form. In the conference committee there was substituted for "unfair competition" the words "unfair methods of competition." This change was made upon the insistence of the House conferees. Senator Cummins, who had introduced the unfair

[1] Cong. Record, September 10, 1914, p. 14928.

[2] On unfair competition, see Nims, Unfair Business Competition.

competition section in the Senate, in discussing the action of the conference committee, said that the two terms in his judgment meant exactly the same thing, though he regretted the change, since the term "unfair competition" was, in his opinion, better understood at law than the term "unfair methods of competition." Representative Covington, chairman of the House conferees, in explaining the conference report, cited numerous cases to show that there was a well-defined class of declarations by the courts defining "unfair methods of competition,"—many more than there were in 1890 to indicate the meaning of the words "contracts in restraint of trade," as found in the Sherman Act. But to meet the objection that the meaning of the law was uncertain it was provided that no penalties should lie against the initial violation of this prohibition; penalties were to operate only after the order of the Commission to desist from the use of any particular unfair competitive device had been affirmed by the courts. In order that meanwhile the use of unfair competitive methods might not prove disastrous to the complainant, provision was made for the expeditious determination of the matter by the courts.

The Senate bill had required the Commission to act whenever it had reason to believe that any person or concern was resorting to unfair competition. The conference committee added a proviso that the Commission should act, "if it shall appear to the commission that a proceeding by it in respect thereof would be to the interest of the public." As Representative Clayton pointed out in explaining the conference report, this proviso was inserted to prevent the Commission from becoming a clearing house for the settlement of everyday quarrels of competitors in matters which were free from detriment to the public, and which ought to be settled through the courts.[1] To compel the Commission to take up every instance of an "unfair method of competition" would hamper it in effecting a speedy redress of those particular unfair competitive methods which tended to bring about monopoly, and which, were they not straightway enjoined, might mean ruin to the independent manufacturers. Unless

[1] Cong. Record, September 10, 1914, p. 14930.

we are to have confidence in the good faith of the Commission in determining when the public interest is concerned, it had been better never to have established such a body. It is particularly important, however, that the Commission act in good faith, since the initiative in preventing unfair competition under this act can be taken only by it; the Department of Justice can not institute a suit to restrain unfair methods of competition; nor can the Court entertain such a suit.

An important change was also made in conference in the nature of the court review of the Commission's orders. The Senate bill had provided that the Commission might bring a suit for the enforcement of its orders in the district court of the appropriate district (the party against whom the order had been given might do the same). In order to avoid the delay of the lower courts, it was provided in conference that the circuit court of appeals should have initial jurisdiction of cases relating to the orders of the Commission, and that the circuit court should expedite the cases in every way possible. The controversy in the Senate between the advocates of a "broad review" of the Commission's orders and a "narrow review" resulted in a victory for the former. The advocates of a "broad review" contended that the Trade Commission Act would be unconstitutional unless it provided for a broad review of the Commission's orders by the courts. A narrow review of the orders of the Interstate Commerce Commission had been held to be constitutional, it was true; but this commission exercised legislative power—the power to prescribe the rates to be charged in the future—and the courts can not interfere with constitutional exercise of legislative power. But the Federal Trade Commission was to have no legislative power; it was to have no power to prescribe fair methods of competition. It was to possess merely the judicial power to order the discontinuance of an unfair method of competition; and under the Constitution the power to act finally in a judicial capacity can be exercised only by a court. The conclusion of the Commission as to the facts was conclusive, but its decision that the facts found constituted a violation of the law had in the nature of the case to be reviewed by the court. Not until the

order of the Commission was sustained did any penalties lie, and even if the Commission was sustained, there were no penalties unless the order of the court was disobeyed. In that event the penalty would be imposed for contempt of court.

The "unfair competition" provisions of the Trade Commission Act should prove very important. The study of individual trusts made earlier in this book has made it clear that unfair competitive methods have proved a powerful weapon in the hands of the trusts to destroy competing enterprises and to discourage potential competitors. In so far as the trusts maintain their position by the use of such tactics, the determined exercise by the Commission of its powers in this respect will go far toward "solving" the trust problem.[1] But while this was probably the purpose of the law, its incidental effects should prove much greater. The law is not limited in its application to trusts or combinations; it applies to all corporations subject to the jurisdiction of the Commission. And perhaps as important, there is legislative approval of the view that ethical principles can be applied to business relationships, that "shrewd" tricks are not to be justified on the ground that "business is business." The commercial world by the acceptance of these principles would make an important stride toward raising the plane of business competition, and toward a marked reduction in the "ruinous" character of competition.

Miscellaneous Provisions

Certain miscellaneous provisions may be noted. It is provided that the Commission or its agents shall at all reasonable times have access to the documentary evidence of any corporation being investigated or proceeded against, with the right to copy such documentary evidence.[2] The penalty for refusal on the

[1] For a copy of the decisions of the Commission dealing with unfair methods of competition, see Federal Trade Commission Decisions, vol. I (covering the period from March 16, 1915, to June 30, 1919). For an enumeration of the methods condemned by the Commission, see Annual Report of the Federal Trade Commission, 1920, p. 56.

[2] Section nine.

part of a corporation is fine or imprisonment, or both.[1] The Commission is given power to require by subpœna the attendance and testimony of witnesses, and the production of all documentary evidence relating to the matter under investigation.[2] In case of disobedience to its subpœna the Commission may invoke the aid of any court of the United States. Failure to obey the order of the court may be punished by the court as a contempt thereof. In another section it is provided that any person who neglects or refuses to attend and testify, or to answer any lawful inquiry, or to produce documentary evidence in obedience to the subpœna or lawful requirement of the Commission, shall be guilty of an offense, and upon conviction thereof by a court shall be subject to a fine of $1,000 to $5,000, or imprisonment for not more than one year, or to both fine and imprisonment.[3] No person may be excused from testifying or from producing documentary evidence on the ground that the testimony or evidence may tend to criminate him, but no natural person shall be prosecuted on account of any matter concerning which he may testify or produce evidence before the Commission in obedience to its subpœna.[4] To prevent any misuse by the employees of the Commission of the information obtained by them in the exercise of their duties and powers, it is provided that any officer or employee of the Commission who shall without authority make public any information obtained by the Commission, unless directed by a court, shall be deemed guilty of a misdemeanor, and be subject to fine or imprisonment, or both.[5] In section eight it is provided that the several departments and bureaus of the government shall, when directed by the President, furnish the Commission, upon its request, all records, papers, and information in their possession relating to any corporation subject to the provisions of the act, and shall detail from time to time such officials and employees as the President may direct; and in the last section (section 11) it is stated that nothing contained in this act shall be construed to interfere with the enforcement of the provisions of the anti-trust acts or the

[1] Section ten.
[2] Section nine.
[3] Section ten.
[4] Section nine.
[5] Section ten.

acts to regulate commerce, nor construed to alter, modify, or repeal these acts or any part thereof.

THE CLAYTON ACT

The Trade Commission Act is a unified measure; it creates a trade commission, and outlines its powers and duties. The Clayton Act, on the other hand, deals with a wide range of matters, a number of which hardly belong in an anti-trust measure. Its leading provisions may be summarized under three headings: first, a set of positive prohibitions dealing with local price discrimination, tying contracts, holding companies, and interlocking directorates; second, remedies; and third, labor provisions. Sections nine and ten, dealing with misconduct on the part of common carriers, it is not proposed to discuss.

Positive Prohibitions

After defining in section one the terms anti-trust laws,[1] commerce,[2] and persons,[3] the act proceeds in sections two, three, seven, and eight, respectively, to prohibit, with certain qualifications, (1) local price discrimination, (2) tying contracts, (3) holding companies, and (4) interlocking directorates. The purpose of these sections, according to the Senate Committee on the Judiciary, was to "make unlawful certain trade practices which, as a rule, singly and in themselves, are not covered by the act of July 2, 1890, or other existing antitrust acts, and thus, by making these practices illegal, to arrest the creation of trusts, conspiracies, and monopolies in their incipiency and before consummation." [4]

[1] Anti-trust laws include, as in the Trade Commission Act, the Sherman Act, sections 73–77 of the Wilson Tariff Act of 1894, and an Act of February 12, 1913, amending sections 73–77 of the Wilson Act; but in addition it includes the Clayton Act itself.

[2] Commerce is defined more broadly than in the Trade Commission Act. It includes insular possessions or other places under the jurisdiction of the United States. The Philippine Islands, however, are excluded. The reasons for the exclusion of the Islands are given in Senate Report no. 698, 63rd Cong., 2nd Sess.

[3] The word persons includes corporations and associations.

[4] Senate Report no. 698, 63rd Cong., 2nd Sess.

(1) Local price discrimination. The detailed study of trusts made in the earlier part of this book has shown the pressing need for federal legislation dealing with local price discrimination. At the time of the passage of this clause at least nineteen separate states had laws prohibiting this form of discrimination.[1] But state legislation is not effective for this purpose, since it does not prevent a trust, doing a nation-wide business, from making its prices uniformly low in a given state in order to eliminate competition in that state, meanwhile recouping itself for the loss thus sustained by charging high prices in the other states. Section two of the act declares "that it shall be unlawful for any person engaged in commerce, in the course of such commerce, either directly or indirectly to discriminate in price between different purchasers of commodities, which commodities are sold for use, consumption, or resale within the United States or any Territory thereof or the District of Columbia or any insular possession or other place under the jurisdiction of the United States, where the effect of such discrimination may be to substantially lessen competition or tend to create a monopoly in any line of commerce: *Provided*, That nothing herein contained shall prevent discrimination in price between purchasers of commodities on account of differences in the grade, quality, or quantity of the commodity sold, or that makes only due allowance for difference in the cost of selling or transportation, or discrimination in price in the same or different communities made in good faith to meet competition: *And provided further*, That nothing herein contained shall prevent persons engaged in selling goods, wares, or merchandise in commerce from selecting their own customers in bona fide transactions and not in restraint of trade."

The House bill had declared that any person engaged in commerce who discriminated in price between different purchasers, "with the purpose or intent thereby to destroy or wrongfully injure the business of a competitor," should be deemed guilty of a misdemeanor and subject to penalty, either fine or imprisonment, or both. The Senate Committee on the Judiciary was of

[1] House Report no. 627, 63rd Cong., 2nd Sess.

the opinion, in view of the experimental character of this legislation, that it would not be wise to apply the harshness of the criminal law; and it therefore struck out the penalty, and put the enforcement of this section in the hands of the Trade Commission.[1] Some two weeks later, however, the Trade Commission Act, conferring upon the Commission power to deal with unfair competition, passed the Senate. As the result of this action, the Committee on the Judiciary recommended that the price discrimination section of the Clayton bill (section 2) be struck out; and this motion was agreed to by the Senate.[2] When the bill went to conference the House conferees objected to the elimination of section two, and for several weeks difficulty was experienced in reaching an agreement. A compromise, however, was finally arrived at. The section was to be restored, but its enforcement was to rest with the Commission, and the criminal penalties provided in the House bill were to be eliminated. The conference committee also accepted the amendment of the Senate Committee on the Judiciary that from the prohibitions of this section there should be excepted price discrimination due to differences in the cost of selling, and price discrimination made in good faith to meet competition. For the House provision that discrimination in price "with the purpose or intent thereby to destroy or wrongfully injure the business of a competitor" was prohibited, the conference committee substituted a prohibition of price discrimination "where the effect of such discrimination may be to substantially lessen competition or tend to create a monopoly in any line of commerce." The report of the conference committee, as has already been pointed out, was approved by both houses without change.

The local price discrimination section has been the subject of much criticism. In particular, objection has been made to the elimination of the penalties. As the act now reads, if a trust resorts to local price cutting which endangers the life of competitors, the Commission *may* enter an order requiring the trust to desist. But, it is said, by the time the order of the Commis-

[1] Senate Report no. 698, 63rd Cong., 2nd Sess.

[2] Cong. Record, August 17, 1914, p. 13849.

sion has been sustained by the courts, the independent concern may have been compelled to abandon the unequal struggle. While the competitor may still sue for and possibly collect damages, nevertheless the competition which the act was passed to preserve would meanwhile have been eliminated. Vigorous objection has also been made to the numerous provisos of the section.[1] A discrimination "made in good faith to meet competition" may seriously interfere with the effectiveness of the prohibition. Can a trust reduce prices in a given locality because an efficient independent concern reduces prices? Undoubtedly it can, for otherwise the trust would be unfairly hampered in competition for business. But may the trust in dealing with this competition merely meet the price of its competitor, or may it reduce prices still further on its own account, reduce them perhaps even below cost? The law appears to place no limitation on the amount of the discrimination when competition is met, unless that is implied in the words "good faith." May not the fear of such destructive action on the part of the trust prevent the independent concerns from initiating any price reductions, and thus insure the maintenance of monopoly prices? Moreover, what discriminations may not be covered up on the ground of differences in grade or quality? Again, what does a "substantial" lessening of competition mean? And may not a trust forbidden to discriminate in prices effect the same end by means of a discrimination in the manner and terms of delivery, or by means of more lenient terms of credit? The objection has been made that section two is surplusage, since local price discrimination is but a form of the unfair competition forbidden in the Trade Commission Act. This, if true, is a minor objection; the important question is, has the prohibition of unfair competition in general been weakened by the specific prohibition of price discrimination subject to numerous and perhaps vital exceptions? Upon these points we must await the decision of the courts.

(2) Tying contracts. The manner in which "tying" contracts

[1] Section two does not forbid the practice of dumping, that is, the sale of commodities abroad at lower prices than at home.

promote monopoly has been described in chapter VIII; and the weakness of state legislation in dealing with this evil in the case of the United Shoe Machinery Company has also been shown. The decision of the Supreme Court in the Dick case (1912) made federal legislation imperative.[1] Section three of the act declares "that it shall be unlawful for any person engaged in commerce, in the course of such commerce, to lease or make a sale or contract for sale of goods, wares, merchandise, machinery, supplies or other commodities, whether patented or unpatented, for use, consumption or resale within the United States or any Territory thereof or the District of Columbia or any insular possession or other place under the jurisdiction of the United States, or fix a price charged therefor, or discount from, or rebate upon, such price, on the condition, agreement or understanding that the lessee or purchaser thereof shall not use or deal in the goods, wares, merchandise, machinery, supplies or other commodities of a competitor or competitors of the lessor or seller, where the effect of such lease, sale, or contract for sale or such condition, agreement or understanding may be to substantially lessen competition or tend to create a monopoly in any line of commerce."

This clause was in substantially this form in the bill as it passed the House. The Senate Committee on the Judiciary—to which the House bill was referred—made three important changes. It eliminated the penalties, and put the enforcement of the section in the hands of the Trade Commission. It made the prohibitions applicable to "contracts for sale" as well as to "sales." And it made the prohibitions applicable to commodities, etc., whether patented or unpatented. All these amendments were accepted in conference, and became part of the law. The Senate, however, did not accept the clause in the form recommended by its committee. Its first act was to strike out this section of the bill entirely,[2] for the same reason that it struck out the price discrimination section. But this action was clearly unwise. The tying contract when used in connection with patented articles would hardly come within the "un-

[1] Cf. p. 419.

[2] Cong. Record, August 17, 1914, p. 13849.

fair methods of competition" prohibited in section five of the Trade Commission Act, since the Supreme Court in the Dick case had upheld a contract of this nature as being within the rights of the patentee under the law as it then stood. The Senate therefore reconsidered its action, and adopted as a substitute for the House section a clause prohibiting with criminal penalties tying contracts in connection with *patented* articles.[1] This amendment, according to Representative Webb, one of the conferees, was evidently aimed at the United Shoe Machinery Company.[2]

The conference committee, after a long discussion, decided to accept the House bill as amended by the Senate Committee on the Judiciary, with one important change. This was to limit the prohibitions of the section to those cases where "the effect of such lease, sale, or contract for sale or such condition, agreement or understanding may be to substantially lessen competition or tend to create a monopoly in any line of commerce." This addition was severely criticized. It was claimed that the term "substantial" was broader than the word "unreasonable" read into the Sherman Act by the Supreme Court; and that it would be difficult to show that competition was "substantially lessened." On the other hand, the section without this qualifying phrase would have prohibited many unobjectionable relationships. Manufacturers frequently sell their goods to dealers on the condition that these dealers will handle their goods only, —a method of disposing of their goods not essentially different from the establishment by the manufacturer of agencies for the sale of goods on a salary or commission basis. If there are a number of dealers in a town this is an effective way—and from the viewpoint of public welfare not an objectionable way—of distributing the product. But if there are only a few dealers—or perhaps only one—then this practice would become objectionable; and it would be prohibited as substantially lessening competition. It was the contracts, leases, etc., that tend to create or maintain monopoly that Congress meant to prohibit;

[1] Cong. Record, August 26, 1914, p. 14276.

[2] Ibid., October 7, 1914, p. 16273.

and these would seem to be prohibited by the clause as it now stands.

(3) Holding companies. The trust movement, as has been shown in chapter IV, was in large measure a holding company movement, and it was therefore to be expected that the trust legislation would deal with holding companies. Moreover, President Wilson in his message to Congress had urged their prohibition. Section seven of the act provides "that no corporation engaged in commerce shall acquire, directly or indirectly, the whole or any part of the stock or other share capital of another corporation engaged also in commerce, where the effect of such acquisition may be to substantially lessen competition between the corporation whose stock is so acquired and the corporation making the acquisition, or to restrain such commerce in any section or community, or tend to create a monopoly of any line of commerce." The second paragraph of this same section (§ 7) contains a prohibition in almost identical language against any corporation (whether engaged in commerce or not) acquiring the stock of two or more corporations engaged in commerce, where the effect of such acquisition, or the use of such stock by the voting of proxies or otherwise, may be to substantially lessen competition, etc. This deals of course with the pure holding company, not itself engaged in commerce.

These prohibitions, which included common carriers, do not, however, apply unfailingly. They do not apply to corporations purchasing such stock solely for investment, and not using the stock to bring about the substantial lessening of competition. They do not prevent corporations engaged in commerce from causing the formation of subsidiary corporations for the actual carrying on of their immediate lawful business, when the effect of such formation is not "to substantially lessen competition." They do not prevent common carriers from constructing or acquiring branch railroads, or extending their lines through the acquisition of stock in other common carriers, when there is no substantial competition between the common carrier and the concern acquired by it. And finally, and more important, nothing contained in this section shall be held "to affect or

impair any right heretofore legally acquired." In other words, this section does not make illegal those holding companies which had been organized in the past for the purpose of creating monopolies. An amendment to this section to make these prohibitions relate to "existing" holdings of stock was introduced by Senator Cummins, but defeated by a vote of 16–37.[1] In order, however, not to legalize the holding companies already organized, it is further provided "That nothing in this section shall be held or construed to authorize or make lawful anything heretofore prohibited or made illegal by the antitrust laws, nor to exempt any person from the penal provisions thereof or the civil remedies therein provided." The holding companies then in existence were thus to retain the status at law which they then had. And that status is one of illegality when the result is an unreasonable restraint of trade or the creation of a monopoly.

(4) Interlocking directorates. The necessity of some legislation to regulate interlocking control of competing companies hardly need be argued. As the House Committee said: "The concentration of wealth, money, and property in the United States under the control and in the hands of a few individuals or great corporations has grown to such an enormous extent that unless checked it will ultimately threaten the perpetuity of our institutions." [2] Section eight of the act provides that after two years no person shall be at the same time a director in two or more corporations engaged in commerce, other than banks [3] and common carriers,[4] any one of which has a capital, surplus, and undivided profits exceeding $1,000,000, if such corporations are or have been theretofore competitors, " so that the elimination of competition by agreement between them would constitute a violation of any of the provisions of any of the antitrust laws." But a director whose election was not prohibited by this act might continue as a director for one year after his election, even

[1] Cong. Record, August 31, 1914, p. 14476.

[2] House Report no. 627, 63rd Cong., 2nd sess.

[3] There were separate provisions dealing with banks.

[4] It was intended to deal with common carriers in the bill regulating the issue of securities; but this bill failed of passage.

though meanwhile there occurred such changes in the affairs of the corporation as would, were it not for this proviso, affect his eligibility to act as a director.

While the courts in various dissolution decrees have enjoined the concerns into which a trust has been dissolved from having common directors, the Clayton Act makes illegal the interlocking of directors among concerns which actually compete, provided that an agreement among these concerns would be illegal. In one respect, therefore, it goes further than the Sherman Act as interpreted by the courts, since the illegality attaches not only to a restraint on competition, but to such relationships as might lead to such restraint.

The Interlocking Directorates bill as originally introduced in the House was very drastic; it declared that the presence of the same individual upon the board of directors of any two corporations engaged in interstate commerce, which by virtue of their location and operation were naturally competitors, would constitute a combination in restraint of commerce subject to all the penalties of the Sherman Act. But the House softened this provision materially, though it voted to retain the criminal penalties. The Senate, however, struck out the criminal penalties; and the bill became law substantially as adopted by it. While undoubtedly the Administration bill was unnecessarily severe, and while the removal of the penalties may have been advisable, it is doubtful whether the law, in so far as it deals with interlocking control, is sufficiently comprehensive. In the first place it deals solely with interlocking directorates. It does not mention interlocking officers or employees, and yet by such devices competition may be quite effectively restrained, not to mention the possibilities of abuse of trust on the part of the officers or employees holding positions in several corporations. It is true that the courts in dissolution decrees have enjoined the segregated companies from having common officers, yet obviously it would be more effective by legislative act to prohibit competing corporations to have common officers (when the elimination of competition by agreement between them would constitute a violation of the antitrust laws), than to secure a

court injunction against this practice after competition has already been restrained. Again, the act does not prohibit interlocking control of competing companies through stock ownership by individuals. So long as the same individual, or group of individuals, controls two potentially competitive concerns, competition will be absent. The fact that these individuals may be prohibited to act as directors in both concerns will not prevent them from exercising control through dummy directors, voting trusts, or otherwise. Neither Congress nor the President seem to have been willing to interfere with the right of an individual to acquire stock in competing corporations, though the President did raise the question for the consideration of Congress. But our experience with the oil and the tobacco trusts has demonstrated that no dissolution which does not prevent the companies into which the trust is divided from being owned by the same group of stockholders is likely to prove effective. Both Attorney Generals McReynolds and Gregory have recognized this fact, and subsequent dissolution suits may therefore prove more effective in this respect. Until Congress also comes to this point of view, its prohibitions will fall short of providing an adequate remedy for the evils with which they deal more or less half-heartedly.

Remedies

The remedies against the unlawful practices previously described may be next considered. Four leading remedies are provided: (1) enforcement through the Federal Trade Commission (or Interstate Commerce Commission or Federal Reserve Board); (2) individual suits for three-fold damages; (3) suits brought by the United States government; (4) individual suits for injunctive relief.

(1) Enforcement through a commission. The Clayton bill as it passed the House punished with criminal penalties any violation of the sections dealing with local price discrimination, tying contracts, holding companies, and interlocking directorates. But in the Senate section two was eliminated, and criminal penalties were removed from sections seven and eight, the

enforcement of these two sections being put in the hands of the Federal Trade Commission and the Interstate Commerce Commission. This was done in order to bring the bill into harmony with the Trade Commission Act, which, as passed by the Senate, gave the Trade Commission jurisdiction over unfair methods of competition in general. The removal of the criminal penalties met with vigorous opposition. It was predicted that litigation to enforce the Commission's orders would be long drawn out, and it was pointed out that even if the Commission should be sustained by the courts no penalties of any kind would accrue. But these protests were unavailing. The conference committee accepted the amendment of the Senate, and on its own account removed the criminal penalty from the Senate section dealing with tying contracts.

The special procedure for the enforcement of sections two, three, seven, and eight of the Clayton Act is found in section eleven. Authority to enforce these sections is vested in the Interstate Commerce Commission, when they apply to common carriers; in the Federal Reserve Board, when they apply to banks and trust companies; and in the Federal Trade Commission, when they apply to other corporations. Instead of proceeding to prevent unfair methods of competition only if a proceeding would be in the interest of the public, as in section five of the Trade Commission Act, these commissions or boards are directed to prevent all violations of these sections. In all other respects the procedure is identical with that provided in the Trade Commission Act for the prevention of unfair methods of competition.

(2) Individual suits for three-fold damages. Section four of the act reënacts with a few minor changes section seven of the Sherman Act. Any person injured in his business or property by reason of anything forbidden in the anti-trust laws may bring suit in any district court of the United States in the district in which the defendant resides or has an agent,[1] and recover three-fold damages, and the cost of the suit.

[1] The words "or has an agent" are not in section seven of the Sherman Act. Their incorporation in the law greatly facilitates the bringing of suits for damages.

This remedy has been given additional effectiveness through a provision in section five of the act "that a final judgment or decree hereafter rendered in any criminal prosecution or in any suit or proceeding in equity brought by or on behalf of the United States under the antitrust laws to the effect that a defendant has violated said laws shall be prima facie evidence against such defendant in any suit or proceeding brought by any other party against such defendant under said laws as to all matters respecting which said judgment or decree would be an estoppel as between the parties thereto;" and through a provision that during the pendency of the government suit the statute of limitations shall be suspended in respect of private rights of action. It was provided, however, that this section shall not apply to consent judgments or decrees entered before any testimony had been taken; nor to any consent judgments or decrees that may be rendered in criminal proceedings or suits in equity, then pending, in which the taking of testimony had been commenced but not concluded, provided such judgments or decrees were rendered before any further testimony was taken.

Section five was designed to facilitate the bringing of suits, particularly by persons of small means, to recover damages for injury sustained on account of a violation of the anti-trust laws. It was in keeping with the recommendation of the President, who in his annual message had said that it was not fair that the private litigant should be obliged to set up and establish again the facts which the government had already proved. The House bill had made the decree of the court conclusive evidence, but the constitutionality of this phrase was attacked, and the conference committee accepted the Senate amendment making the decree of the court prima facie evidence. Consent decrees were exempted from a fear that otherwise concerns charged with violating the law would refuse to consent to a voluntary readjustment of their affairs, preferring instead to take their chances on a favorable court decision. The Senate bill had provided that final decrees "heretofore rendered," as well as those hereafter rendered, should be prima facie evidence, but this was struck out in the conference committee. The exclusion of these words was

criticized in the Senate as showing special tenderness to the Standard Oil and other trusts, evidence against which had been secured by the government with great difficulty and at great expense.

(3) Suits brought by the United States government. Section fifteen of the act invests the district courts of the United States with jurisdiction to prevent and restrain violations of the act, and makes it the duty of the district attorneys of the United States, in their respective districts, under the direction of the Attorney General, to institute proceedings to enforce the act. This section is identical with sections four and five of the Sherman Act, except that jurisdiction is vested in the district courts rather than in the circuit courts, the latter having been abolished in 1911.

The United States government through the Department of Justice has jurisdiction, it should be observed, over all violations of the act, including violations of sections two, three, seven, and eight. With respect to these sections, therefore, the Department of Justice shares jurisdiction with the Federal Trade Commission, the Interstate Commerce Commission, and the Federal Reserve Board. Whether this will lead to friction between these government agencies remains to be seen.

In dealing with violations of the act the hands of the government are strengthened by section fourteen, which, in line with the recommendation of the President, makes guilt personal. This section declares " that whenever a corporation shall violate any of the penal provisions of the antitrust laws, such violation shall be deemed to be also that of the individual directors, officers, or agents of such corporation who shall have authorized, ordered, or done any of the acts constituting in whole or in part such violation," and such violation shall subject the director, officer, or agent to the penalty of a fine not exceeding $5,000, or to imprisonment for a period not to exceed one year, or to both, in the discretion of the court.

The "personal guilt" section applies only to the *penal* provisions of the anti-trust laws, which limits it to sections one to three of the Sherman Act, section seventy-three of the Wilson

Tariff Act of 1894 as amended in 1913, and sections nine and ten of the Clayton Act. As this section passed the House it applied to *any* violation of the anti-trust laws. But in the Senate the word penal was inserted, and the penalties were eliminated except from section three, dealing with tying contracts. These changes being accepted in conference (the conference committee on its own account took out the penalties from section three), the net result was to limit greatly the scope of this section. Whether the result was also to reduce its effectiveness depends on the relative merits of criminal and civil remedies. Were juries willing to convict, undoubtedly the criminal remedies would be the more effective; but as a matter of fact, juries have shown a reluctance to apply the harsher remedy. Perhaps, now that the anti-trust laws have been affirmed and the provision for personal guilt inserted, they will become more stern in this regard. On the other hand, in some respects civil remedies are more effective. In a criminal prosecution suit may be brought only by the Department of Justice, and guilt must be established beyond a reasonable doubt; whereas in a civil action any one can bring suit, and a preponderance of evidence suffices.

(4) Individual suits for injunctive relief. Section sixteen provides that any person or concern is entitled to injunctive relief, in any court of the United States having jurisdiction over the parties, against threatened loss or damage by a violation of the anti-trust laws, including sections two, three, seven, and eight of the Clayton Act; and that a preliminary injunction is to be issued upon a showing that the danger of irreparable damage is immediate, and upon the execution of a bond against damages for an injunction improvidently granted, provided, that only the United States may bring suit for injunctive relief against common carriers. The express provision that the new method of relief is to apply to sections two, three, seven, and eight, shows conclusively that the remedy of Commission enforcement provided in section eleven is cumulative in character and not exclusive.

Section sixteen gives the person or concern injured in his (or its) business a remedy that it had not possessed before. For-

merly only the United States government, under the direction of the Attorney General, could enjoin a violation of the anti-trust act; and if the Attorney General was negligent no injunctive relief could be had. As the law now stands an independent concern attacked through some unfair device may secure an injunction against the employment of this device, and thus protect its existence, rather than sue for damages, as formerly, after injury and perhaps bankruptcy had resulted. In addition, the business public becomes the ally of the Government in enforcing the anti-trust laws.

Reference may also be made to section twelve, which liberalizes the procedure in the courts by providing that suit under the anti-trust laws against a corporation may be brought, not only in the judicial district whereof it is an inhabitant, as under the law previously, but also in any district where it may be found or transact business. This clause makes it easier to bring suit, since it largely does away with long distance litigation, and thus decreases the expense to the plaintiff.

The possibility that the whole act will be rendered invalid by reason of the unconstitutionality of any part thereof is eliminated by the provision that the judgment by any court of competent jurisdiction that any clause, sentence, paragraph, or part of the act is invalid is not to impair or invalidate the remainder of the act.[1] A similar provision had been inserted in the Tariff Act and the Federal Reserve Act, both enacted the previous year.

Labor Provisions

The Clayton Act contains a number of provisions much desired by labor organizations. Thus section twenty limits the use of the injunction in labor disputes, and appears to legalize strikes, picketing, and boycotts.[2] And section six declares "that the labor of a human being is not a commodity or article of commerce. Nothing contained in the antitrust laws shall

[1] Section twenty-six.

[2] But see the decision of the Supreme Court in the Duplex Printing Press Company case, 254 U. S. 443. (January 3, 1921).

be construed to forbid the existence and operation of labor, agricultural, or horticultural organizations, instituted for the purposes of mutual help, and not having capital stock or conducted for profit, or to forbid or restrain individual members of such organizations from lawfully carrying out the legitimate objects thereof; nor shall such organizations, or the members thereof, be held or construed to be illegal combinations or conspiracies in restraint of trade, under the antitrust laws.

This section, together with section twenty, has been acclaimed as constituting a bill of rights for labor. While there is some doubt as to the interpretation which these provisions will receive at the hands of the courts, there is no doubt that organized labor considers that it has won a great victory. President Gompers, of the American Federation of Labor, has said that the declaration that the labor of a human being is not a commodity or article of commerce "is the Industrial Magna Carta upon which the working people will rear their structure of industrial freedom." [1] On the other hand, an economist of note refers to this declaration as an "empty blague." [2] The provisions that nothing contained in the anti-trust laws shall be construed to forbid the existence and operation of labor organizations, and that these organizations, or their members, shall not be held to be illegal combinations or conspiracies in restraint of trade under the anti-trust laws apparently removes doubt as to the legality of such organizations,—organizations which formerly, according to Mr. Gompers, existed only on the sufferance of the administration.[3] The above provisions apply likewise to agricultural and horticultural organizations not having capital stock or conducted for profit. However, unlike the labor organizations, many agricultural organizations have capital stock, and most of them are conducted for profit; [4] and therefore this exemption will not be likely to have such broad consequences as the exemption of labor organizations, unless indeed

[1] American Federationist, 21, pp. 971–2 (November, 1914).
[2] Young, Journal of Political Economy, 23, p. 418.
[3] House Report no. 627, 63rd Cong., 2nd Sess.
[4] Ibid.

the courts hold that the latter are conducted for profit. The provision that nothing in the anti-trust laws shall be construed to forbid or restrain individual members of labor and agricultural organizations from "lawfully carrying out the legitimate objects thereof" would appear to be meaningless. It is difficult to conceive of a law forbidding an organization from *lawfully* carrying out its *legitimate* objects.

CHAPTER XVI

THE WEBB-POMERENE ACT [1]

The only important anti-trust legislation enacted since 1914 is the Webb-Pomerene Act, designed to promote the American export trade through the legalization of export associations. It is proposed in this chapter to outline briefly the conditions that gave rise to a demand for such legislation; to trace the progress of the bill through Congress; to describe the provisions of the act; and to call attention to some possible objections. First as to the conditions that led to the passage of the Webb Act.

During the early years of the twentieth century it was freely predicted that American manufacturers, combined as many of them were in the modern trust, were to capture the markets of the world. Only a few years later the opinion was as commonly expressed that without legislation permitting coöperation in the American export trade our manufacturers were no match for their foreign competitors. Several reasons were given for the unequal conditions of competition. In the first place, American manufacturers in striving for business abroad had to meet the vigorous rivalry of powerful foreign combinations, often international in scope. These combinations were frequently aided by their respective governments, and in some cases participated in by these governments. The stock illustration was Germany, which had achieved the most notable success in the

[1] On the Webb-Pomerene Act see: Congressional Record, vols. 53–56; Report of the Federal Trade Commission on Cooperation in American Export Trade, in two parts; House Report no. 1118, 64th Cong., 1st sess.; Senate Report no. 1056, 64th Cong., 2nd sess.; House Report no. 50, 65th Cong., 1st sess.; Proceedings of the National Foreign Trade Conventions; Duncan, Journal of Political Economy, 25, pp. 313–338 (1917); Notz, Journal of Political Economy, 27, pp. 525–543 (1919); and Notz, Yale Law Journal, 29, pp. 29–45 (1919).

rapid development of its foreign trade and which, being highly unpopular after 1914, furnished a good talking point. However, such combinations were common in other countries, for example, Belgium, Holland, Italy, and Japan. In Great Britain, on the other hand, despite the absence of widespread combination, a large and profitable export trade was being maintained. This was attributed to the unusually favorable conditions, notably the advantage of an early start, the possession of excellent shipping and banking facilities, and the high grade of service rendered by the British commission merchants, not to mention the export houses buying and selling goods for export on their own account. Some American companies, particularly the United States Steel Corporation, the Standard Oil Company, and the International Harvester Company, were admittedly strong enough to cope with these foreign combinations, yet the smaller concerns in these industries, as well as nearly all of the concerns in certain industries in which competitive conditions prevailed, were said to be at a great disadvantage. Hence the need of association.

Secondly, in the leading countries of the world associations for the promotion of export business were permitted,—an advantage that the Sherman Act denied, so it was believed, to American exporters. In Germany, for example, prior to the war there were 600 important cartels, many of which dominated the export trade in their particular industry.[1] These cartels made an especial effort to extend the foreign trade, frequently selling at a loss in the endeavor to gain a foothold or to maintain a position once established. In order that such agencies might be met on more equal terms the association of American manufacturers in a common selling agency was held to be necessary. The need for such association, it may be observed, was not equally great in all branches of the export trade. Thus, American foodstuffs and raw materials could readily be sold even without an export organization, though coöperation might

[1] Report of the Federal Trade Commission on Cooperation in the American Export Trade, I, p. 5. Hereafter referred to as Report on Cooperation in American Export Trade.

somewhat reduce the cost of distribution, and might increase the bargaining power of American producers. There was even less occasion for association of the manufacturers of specialties. Here the lack of standardization would make difficult the work of an export organization. Moreover, less competition was encountered in the sale of specialties, such as safety razors, for example, and as a result coöperation was not so important. Of course, the exporters of specialties also had to create their market abroad, but many of them had found it to their advantage to do this individually. It was in the manufactured staples that the advantages of coöperation were most marked. Such goods met vigorous competition abroad, often at the hands of large organizations. To capture foreign trade under such circumstances it was usually necessary to study the foreign requirements; to employ salesmen familiar with foreign conditions and customs; to advertise and demonstrate; to keep in touch with credit conditions, so that credit might be extended wisely; to establish abroad branches and warehouses in order that the foreign customer might count on prompt and regular deliveries; in a word, to maintain an effective system of direct representation.

Even in the foreign trade in manufactured staples export associations were not always necessary or even advantageous. In many branches there existed highly efficient export commission houses handling sales on a commission basis, and export merchants buying and selling goods on their own account. These agencies in both Great Britain and the United States had played a notable part in the development of export trade. In fact, British export trade had been largely built up through their efforts.[1] These export houses had already developed efficient organizations, which were familiar with foreign conditions; and they now possess an advantage over associations in this country by virtue of the fact that they handle imports as well as exports, whereas the American associations under the provisions of the Webb Act may deal solely in exports. For the export houses, owning their own ships, as many of them do, the han-

[1] See Report on Cooperation in American Export Trade, I, p. 94; II, p. 320.

dling of imports as well as exports represents an undoubted saving in transportation, in that it more commonly provides a cargo in both directions. However, the system of direct representation also has its advantages. Thus it is to be anticipated that the foreign trade in any particular article, and of course the domestic trade also, will be more effectively pushed by an agency whose capital is invested in plants and equipment devoted to the manfacture of that product than by an agency having no such investment and dealing in a great variety of products. An association obviously has an individual interest in its product, an interest which an export house in the very nature of the case lacks.

Thirdly, in some of the foreign markets American producers were confronted with well organized combinations of buyers. Thus, four London concerns were said to fix the price of silver, and American exporters in making sales in Great Britain, India and elsewhere had to accept the price fixed by these firms.[1] For some time past the world's copper trade had been controlled by a German metal-buying agency.[2] Such associations, it was said, by playing off one American exporter against another were able to beat down the price of American goods destined for export. In the case of copper the aforementioned German concern, according to Mr. John D. Ryan, president of the Amalgamated Copper Company, by means of such tactics bought American copper delivered abroad during 1903 to 1913 at 83/100 of a cent per pound less than domestic buyers paid for delivery at New York or the Connecticut Valley.[3] The association of American producers in a selling agency, it was claimed, would eliminate the competition between American firms, and thus make it possible for them to secure better prices for articles sold abroad.

Finally, the development of our export trade was said to be hampered by inadequate banking and credit facilities abroad; by discrimination against American goods by foreign steamship lines; by the small amount of American investments in the securities of foreign companies; and by our comparative inex-

[1] Report on Cooperation in American Export Trade, I, p. 7.
[2] Ibid., p. 7.
[3] Ibid., II, p. 261.

perience. The last obstacle perforce had to be overcome by the producers and manufacturers themselves. Upon them necessarily fell the task of developing the requisite organization, of acquiring an intimate acquaintanceship with the requirements of foreign markets, and by attention to quality and service of creating a demand for products "Made in America." The additional business that comes through investments in foreign enterprises was to be secured by a campaign to educate American investors in the advantages of foreign securities,—a campaign now well under way. The other difficulties were to be met by legislation permitting foreign banking, establishing an American merchant marine, and authorizing producers and manufacturers to combine for export purposes. The Webb bill was thus only one stone in the foundation upon which our increased foreign trade was to rest.

The desirability of legalizing associations for export trade was inquired into by the Federal Trade Commission under the powers granted to it in § 6 (h) of the Trade Commission Act, and a decision highly favorable to the principle underlying the Webb Act was reached.[1] The Commission pointed out that such large concerns as the United States Steel Corporation, the International Harvester Company, the United Shoe Machinery Company, the National Cash Register Company, the General Electric Company and others did not need to enter into export associations, since they individually were well able to compete with foreign combinations.[2] Rather the purpose of the Webb bill was to enable a number of smaller companies not having a large enough volume of business to justify the carrying on of an export trade by themselves to coöperate for this purpose and, by distributing the overhead charges over their combined foreign sales, to bring the costs down to a reasonable figure. Other advantages to be gained through coöperative action were the securing of better credit information and thus the better financing of foreign business, an ability to give longer credits when desirable, the greater ease with which initial losses could be carried, a larger

[1] See Report on Cooperation in American Export Trade, I, p. 379.

[2] Ibid., pp. 161–162, 242.

assortment of goods, and the exchange of ideas among the members of the association. While there is some reason to believe that an association of competing concerns to share the expenses of a foreign selling agency was not in fact prohibited by the anti-trust laws,[1] provided it did not embrace too large a percentage of the trade, nevertheless the uncertainty as to the legal status of such an arrangement had deterred many concerns that were anxious to coöperate from making the venture. The Commission after a study of the legal aspects of the problem was unable to assure manufacturers that common selling agencies were lawful; and accordingly it recommended the passage of an act that would place this right beyond dispute. This recommendation was made, however, subject to the condition that ample precautions be taken to prevent the export associations from being used to restrain trade in the United States in violation of the Sherman Law.[2]

The campaign to legalize export associations was launched at the first convention of the National Foreign Trade Council, held in Washington, D. C., toward the close of May, 1914. There was thus no connection between the initiation of this movement and the European war. However, the outbreak of the war on August 1, 1914, followed as it was by a short period of depression in this country, presented conditions favorable for an agitation to legalize combinations for the export trade,—it being alleged that foreign business was necessary to "keep the home fires burning" and to provide employment for labor. In May, 1915, the Federal Trade Commission, organized only two months previously, began an investigation of the foreign trade with particular reference to the advisability of permitting coöperation. A summary of its findings, made public in May, 1916, strongly recommended the enactment of permissive legislation.[3] At the

[1] Some such associations, believed to be legal, had been organized prior to the passage of the Webb Act. See Official Report of the Fourth National Foreign Trade Convention, 1917, p. 187.

[2] Report on Cooperation in American Export Trade, I, p. 10.

[3] The full report, in two volumes, though dated June 30, 1916, was not published until December, 1916.

date of this report a vast foreign trade was being carried on, and there was no immediate occasion for concern on this score. The campaign cry was thus modified to meet the new situation. Attention was now directed to the tremendous struggle for foreign trade that would manifest itself upon the conclusion of hostilities, and the country was urged by the interested parties to have its loins girded for the fray when it arrived.

The Webb bill was first introduced in the House by Representative Webb of North Carolina on August 8, 1916, some three months after the publication of the summary of the report of the Federal Trade Commission. It was referred to the Committee on the Judiciary, of which Mr. Webb, who had so skilfully and tactfully piloted the Clayton Act through the House two years previously, was chairman. After being amended in important particulars, the significance of which will be noted later,[1] it passed the House on September 2 by a vote of 199–25.[2] Six days later the Senate adjourned; and the Webb bill was permitted to slumber in committee.

President Wilson in his address to the next Congress on December 5, 1916, urged the prompt passage of the Webb bill. He presented no argument on behalf of the bill, but merely pointed out that a great opportunity in foreign trade had presented itself, and that this opportunity might escape us if we hesitated or delayed to remove the legal obstacles that stood in the way.

Notwithstanding the recommendation of the President the Webb bill made practically no progress during the short session from December 4, 1916, to March 4, 1917. The Senate Committee on Interstate Commerce, of which Senator Pomerene was chairman, reported out the bill on February 16, 1917, with amendments, but the measure was not discussed in either the Senate or the House.

During the next session (April 2, 1917–October 6, 1917) the bill in amended form passed the House for the second time, but did not come to a vote in the Senate. The bill as reported out by the House Committee on the Judiciary on May 11, 1917, was

[1] See p. 382.

[2] Cong. Record, September 2, 1916, p. 13732.

revised in several important particulars to conform to the suggestions of the Senate Committee on Interstate Commerce. As revised by the House Committee, but without any further changes, it passed the House on June 13 by a vote of 242–29, having been debated on only one day, the day of its passage.[1] The measure was briefly debated in the Senate on three separate days, but it was not put to a vote, Senator Pomerene having concluded after an investigation that it was impossible to secure action during the current session.

With the convening of the second session of the 65th Congress President Wilson on December 4, 1917, again called the attention of Congress to the Webb bill, saying it "ought by all means to be completed at this session."[2] On this occasion the Senate was prompt indeed. It debated the measure for four days, and on December 12 accepted it, slightly amended, by a vote of 51–11.[3] The House objected to the Senate amendments, and conferees were therefore appointed. The report of the conference committee was presented on April 2, 1918; and was accepted by both the Senate and the House on April 6. The bill was signed by the President on April 10.

The act is divided into five sections. Section one is devoted to a definition of certain terms used in the act. The word "association" is defined as "any corporation or combination, by contract or otherwise, of two or more persons, partnerships, or corporations." The words "export trade" mean "solely trade or commerce in goods, wares, or merchandise exported, or in the course of being exported from the United States or any Territory thereof to any foreign nation; but . . . shall not be deemed to include the production, manufacture, or selling for consumption or for resale, within the United States or any Territory thereof, of such goods, wares, or merchandise, or any act in the course of such production, manufacture, or selling for consumption or for resale."[4]

[1] Cong. Record, June 13, 1917, p. 3584.

[2] Ibid., December 4, 1917, p. 20.

[3] Ibid., December 12, 1917, p. 186.

[4] In the opinion of the Federal Trade Commission, trade with the Philip-

The bill as it had passed the House on September 2, 1916, instead of providing that "export trade" should not be deemed to include the production, manufacture, *or selling for consumption or for resale* within the United States of exported goods, had provided that it should not be deemed to include the production, manufacture, *trading in, or marketing* within the United States of such goods.[1] In this form obviously the measure was highly unsatisfactory to those desiring to form export associations; for unless an export association could either produce or trade in, that is, buy, the articles to be exported, its activities would be limited to handling goods on a commission or agency basis, if indeed that was permissible. If it was deemed advisable to allow export associations there was no virtue in unduly hampering them; and accordingly the Senate struck out the words "trading in, or marketing," and substituted the words "or selling for consumption or for resale." By these changes, concurred in by the House, an export association was permitted to purchase goods in this country for export purposes, but it might not produce them itself nor sell them in this country.

Section two provides that nothing in the Sherman Act of 1890 "shall be construed as declaring to be illegal an association entered into for the sole purpose of engaging in export trade and actually engaged solely in such export trade, or an agreement made or act done in the course of export trade by such association, provided such association, agreement, or act is not in restraint of trade within the United States, and is not in restraint of the export trade of any domestic competitor of such association: *And provided further*, That such association does not, either in the United States or elsewhere, enter into any agreement, understanding, or conspiracy, or do any act which artificially or intentionally enhances or depresses prices within the United States of commodities of the class exported by such

pine Islands, Porto Rico, and Hawaii is not export trade. Annual Report, 1918, p. 40.

[1] See text of bill in Annual Report of the Federal Trade Commission, 1916, pp. 60–61.

association, or which substantially lessens competition within the United States or otherwise restrains trade therein."

Section two of the act as above quoted is identical with the bill as it first passed the House down to the words "in restraint of trade within the United States;" but differs vitally from that point on. The House bill had legalized export associations provided they were not in restraint of trade within the United States, and provided they did not *restrain the export trade of the United States.*[1] The Senate Committee on Interstate Commerce pointed out that this second proviso took away a right granted elsewhere in the bill to enter into associations and make agreements in restraint of export trade; and it accordingly modified the proviso so that it merely forbade a restraint of the export trade *of any domestic competitor of such association.*[2] This change was accepted by the Senate and the House. Having removed, however, the prohibition against the restraint of the export trade of the United States, it became necessary to provide in some way against the use of such associations to influence prices improperly in this country. Accordingly the Senate Committee added the last proviso dealing with prices in the United States. The bill as it became law is identical with the amendment of the Senate Committee except in three particulars: (1) the Senate inserted the words "or depresses" after "enhances" in order to prevent export associations from beating down the prices of goods purchased by them;[3] (2) the Senate struck out the words "and unduly" enhances prices, from an uncertainty as to the meaning of "undue" enhancement;[4] and (3) the conference committee added the words at the close of section two reading "or which substantially lessens competition within the United States or otherwise restrains trade therein."

[1] This second proviso was not in the bill as originally introduced in the House by Mr. Webb, but he agreed to the change. See Cong. Record, September 2, 1916, p. 13725.

[2] See Senate Report no. 1056, 64th Cong., 2nd Sess.

[3] Cong. Record, May 23, 1917, p. 2787; and September 22, 1917, p. 7325.

[4] Ibid., December 12, 1917, p. 184.

Section three amends section seven of the Clayton Act by providing that any corporation may acquire all or part of the stock or other capital of any company organized in accordance with the terms of the Webb Act, "unless the effect of such acquisition or ownership may be to restrain trade or substantially lessen competition within the United States."

Section four declares that the provisions of the Trade Commission Act with regard to unfair methods of competition "shall be construed as extending to unfair methods of competition used in export trade against competitors engaged in export trade, even though the acts constituting such unfair methods are done without the territorial jurisdiction of the United States." This section extends the jurisdiction of the Federal Trade Commission over unfair competition to foreign trade as well as to domestic; and is in line with a recommendation of that body in its report on Cooperation in American Export Trade.[1] The prohibition of unfair competition, it should be observed, relates only to methods used against *American* competitors engaged in export trade. The section says, to be sure, competitors engaged in export trade, without qualification, yet since export trade is defined as trade in goods exported from the United States, it is clear that it applies only to American competitors. The provisions of section four are applicable not only to associations, but also to corporations and individual exporters.

Section five provides that every association organized under the act shall file with the Federal Trade Commission a statement giving certain information, including the location of its offices, the names and addresses of all of its officers, stockholders, or members, and a copy of its articles of incorporation or association; and that on January first of each year a similar statement, noting changes, if any, shall be made. Every association "shall also furnish to the commission such information as the commission may require as to its organization, business, conduct, practices, management, and relation to other associations, corporations, partnerships, and individuals." Any association failing to comply with these requirements is to be denied the benefits

[1] I, p. 380.

of sections two and three of the act, and to be subject to a fine of $100 per day to be recovered by the Attorney General.

The foregoing provisions are substantially as in the original House bill, except for the clause, inserted in the Senate, permitting the Commission to inquire into the organization, business, etc., of export associations. But because of its amendments to section two, dealing with the effect of export associations on prices or competition in the United States, the Senate deemed it advisable to add another paragraph to section five, establishing administrative machinery for the enforcement of the restrictions imposed in section two. It accordingly provided that whenever the Federal Trade Commission had reason to believe that the provisos of section two had been violated, it should conduct an investigation; and if upon investigation it concluded that the law had been violated "it may make to such association recommendations for the readjustment of its business, in order that it may thereafter maintain its organization and management and conduct its business in accordance with law." If the association fails to comply with the recommendations of the Federal Trade Commission, the latter is to refer its findings and recommendations to the Attorney General for such action as he may deem proper. This paragraph was accepted by the House.

In the House an attempt had been made to require associations desiring to benefit by this act to secure a permit from the Federal Trade Commission; and to authorize the Commission to refuse such permits, and once having issued them to cancel them for cause after a hearing. The author of this amendment took the position that, if permits were required, and were held subject to good behavior, administrative supervision would be effective, as it would not be if offenders had to be haled into court. The objection was made that this would vest a dangerous power in the Commission, and the proposition was rejected by a vote of 131–11.[1]

A third and final paragraph gave the Commission in the enforcement of these provisions all the powers, where applicable,

[1] Cong. Record, June 13, 1917, pp. 3578, 3580, 3584.

given it in the Trade Commission Act of September 26, 1914.

The advantages of export associations have been stated. We may now consider some of the possible disadvantages.

The chief objection to the export associations authorized by the Webb Act is that they may be used as a means of restricting competition in the domestic market. The Federal Trade Commission recognized this danger, but expressed the opinion that it would be possible through administrative supervision to prevent these organizations from being employed in this fashion. Others, however, doubt whether this is possible. If all the concerns in a given industry are associated in a common enterprise, they will tend to draw together and to pursue a harmonious policy with regard to domestic business. The Gary dinners in the steel trade were a remarkably effective device in maintaining a policy of coöperation that was equivalent to the fixing of prices. These dinners were illegal, and they were discontinued. However, meetings of these same groups through the medium of an export association are not illegal; and it will be exceedingly difficult, if not impossible, to prevent some understanding being arrived at with regard to domestic prices and output. This is the more true, since the export associations will naturally fix export prices, and an agreement as to the relationship between export and domestic prices can readily be effected. Whether or not it be true, as alleged by the minority of the House Committee on the Judiciary, that the Webb legislation was sought "not so much for its value in the foreign trade as for the effect it would have on the domestic trade," [1] it is hardly to be doubted that a restraint of domestic trade will be the practical result in some, if not numerous, instances.

A second possibility is that the Webb Act will promote international combination. Even prior to the enactment of this measure there had been international combinations in steel rails, gunpowder, tobacco, thread, and other products, the underlying purpose of these combinations being the maintenance of an undisputed position in the domestic market. So far as the

[1] House Report no. 50, 65th Cong., 1st sess.

United States is concerned these arrangements will now be legal, since such restrictions as the Sherman Act imposed on restraints of foreign trade are now removed, providing the restraint of the export trade does not restrain trade within the United States, and does not restrain the export trade of a domestic competitor of the export association. It is also to be anticipated, the provisos in section two to the contrary notwithstanding, that the effect of an extension of international combination will be to reduce the effectiveness of foreign competition in this country, that is, where the absence of a protective tariff has permitted such competition to exist.

Another result of the organization of export combinations in the United States may be a further extension of foreign combinations, in order that foreign buyers may be in a position to bargain effectively with American export sales agencies. The ultimate consequences of pitting a single American seller against a single foreign buyer in each country, if it should come to that, are not easy to foresee, yet it is clear that there exists the possibility of prolonged negotiations during the pendency of which the export trade will greatly suffer.

Finally, there is danger lest the pursuit of trade by large groups will tend to upset once more the peace of the world. The House Committee on the Judiciary, in advocating the passage of the Webb bill, declared that export trade, by virtue of the methods adopted by other leading countries, had become "largely a matter of competition between nations."[1] If the Government of the United States is to become a party to this international rivalry for trade, it must be in a position to support its foreign trade agencies by force of arms, if necessary, with consequences that may easily be foreseen by any one who has learned the lessons of the recent war. It may be, however, that it is not necessary for us to run these risks, particularly in view of the insistent demand abroad for American products, and in view of the immense proportions of our domestic trade.

[1] House Report no. 1118, 64th Cong., 1st sess.

CHAPTER XVII

JUDICIAL INTERPRETATION OF THE SHERMAN ACT

We come now to the interpretation of the Sherman Anti-trust Act by the courts. No attempt is here made to consider all the cases involving the Sherman Act that have arisen in the courts; only the leading cases that are significant for the purposes of this book are treated.[1] Generally speaking, reference is made only to the decisions of the Supreme Court, though in two instances—the harvester and the glucose cases—the decisions of the lower courts are briefly outlined.

UNITED STATES *v.* E. C. KNIGHT COMPANY [2]

The first case to come before the Supreme Court was United States *v.* E. C. Knight Company. In 1892 the American Sugar Refining Company, producing about 65 per cent of all the sugar refined in the United States, had purchased control of E. C. Knight Company and three other independent sugar refining companies, producing among them some 33 per cent of the country's output of refined sugar.[3] The government charged that the contracts under which these purchases had been made constituted combinations in restraint of trade; and it brought suit to compel their cancellation. Both the Circuit Court [4] and the Circuit Court of Appeals [5] ordered the suit dismissed. Thereupon an appeal was taken to the Supreme Court.

The Supreme Court in its decision rendered on January 21, 1895, sustained the lower courts. "The fundamental question,"

[1] For a topical analysis of the leading cases that have arisen under the Sherman Act, see the report of the Commissioner of Corporations on Trust Laws and Unfair Competition, pp. 70–123.

[2] 156 U. S. 1–46 (January 21, 1895).

[3] See p. 93.

[4] 60 Fed. Rep. 306.

[5] Ibid., 934.

said the Court, "is, whether conceding that the existence of a monopoly in manufacture is established by the evidence, that monopoly can be directly suppressed under the act of Congress in the mode attempted by this bill." The argument which was advanced by the government was, to use the Court's summary, that "the power to control the manufacture of refined sugar is a monopoly over a necessary of life, to the enjoyment of which by a large part of the population of the United States interstate commerce is indispensable, and that, therefore, the general government in the exercise of the power to regulate commerce may repress such monopoly directly and set aside the instruments which have created it." With reference to this argument the Court said: "Doubtless the power to control the manufacture of a given thing involves in a certain sense the control of its disposition, but this is a secondary and not the primary sense; and although the exercise of that power may result in bringing the operation of commerce into play, it does not control it, and affects it only incidentally and indirectly. Commerce succeeds to manufacture, and is not a part of it. The power to regulate commerce is the power to prescribe the rule by which commerce shall be governed, and is a power independent of the power to suppress monopoly."[1] And by the act of July 2, 1890, Congress did not attempt "to assert the power to deal with monopoly directly as such. . . . What the law struck at was combinations, contracts, and conspiracies to monopolize trade and commerce among the several States or with foreign nations; but *the contracts and acts of the defendants related exclusively to the acquisition of the Philadelphia refineries and the business of sugar refining in Pennsylvania, and bore no direct relation to commerce between the States or with foreign nations*[2] . . . . It is true that the bill alleged that the products of these refineries were sold and distributed among the several States, and that all the companies were engaged in trade or commerce with the several States and with

[1] However, the power to regulate commerce "may operate in repression of monopoly whenever that comes within the rules by which commerce is governed or whenever the transaction is itself a monopoly of commerce."

[2] Italics supplied by the author.

foreign nations; but this was no more than to say that trade and commerce served manufacture to fulfil its function. . . . *There was nothing in the proofs to indicate any intention to put a restraint upon trade or commerce,*[1] and the fact, as we have seen, that trade or commerce might be indirectly affected was not enough to entitle complainants to a decree."

A vigorous dissenting opinion was rendered by Justice Harlan, who discussed the legal aspects of the case fully. With respect to the economic effects of the decision, he held that freedom of commercial intercourse embraces the right to buy goods to be transported from one state to another, without buyers being burdened by unlawful restraints imposed by combinations or corporations or individuals; and that if this principle were not adhered to, "interstate traffic, so far as it involves the price to be paid for articles necessary to the comfort and well-being of the people in all the States, may pass under the absolute control of overshadowing combinations having financial resources without limit and an audacity in the accomplishment of their objects that recognizes none of the restraints of moral obligations controlling the action of individuals; combinations governed entirely by the law of greed and selfishness—so powerful that no single State is able to overthrow them and give the required protection to the whole country, and so all-pervading that they threaten the integrity of our institutions."

He then went on to inquire (a significant inquiry in the light of the subsequent course of events) how the people of the United States were to be protected against combinations to fix the price of flour, grain, oil, salt, cotton, and meat—should such be organized—except by a national power, a power capable of exerting its sovereign authority throughout every part of the territory, and over all the people of the nation.

The decision of the Supreme Court in the Knight case apparently limited greatly the power of the federal government to deal with trusts and monopolies. That this decision stimulated the formation of trusts in 1897 as soon as industrial conditions made their organization by the promoters feasible—thus realiz-

[1] Italics supplied by the author.

ing the fears of Justice Harlan—is undoubted. Yet later decisions by the Supreme Court have shown that the Sherman Act is by no means as ineffective to carry out the purpose for which it was designed as the decision in the Knight case would have led one to suppose. The explanation, in part at least, is that the Knight case was not properly presented, and therefore the decision of the Supreme Court in this case did not bring out the real scope of the law. What the Sherman Act declares illegal is the restraint and monopoly of interstate and international commerce, but, as the Supreme Court pointed out, there was nothing in the *proofs* in the Knight case to indicate an intention to put a restraint upon trade or commerce. It is hardly necessary to say that the Supreme Court in deciding the case was perforce confined to the record submitted. If the record was inadequate, the responsibility for the failure to sustain the government must be laid at the door of the Attorney General, and not at that of the Supreme Court.

UNITED STATES *v.* TRANS-MISSOURI FREIGHT ASSOCIATION [1]

This decision is important in that it established that the Sherman Act applied to *all* contracts in restraint of trade, including those between railroad companies.

On March 15, 1889, a number of railway companies, engaged in interstate commerce, formed an association, known as the Trans Missouri Freight Association, the purpose of which was stated to be the establishment and maintenance of reasonable rates, rules, and regulations on interstate freight traffic south and west of the Missouri river. The Sherman Act was subsequently passed on July 2, 1890, but the association maintained its existence without change. The government thereupon brought a suit in equity to have the association dissolved.

The defendants claimed that the Sherman Act did not apply to railroads, and that even if it did, the agreement was reasonable, and therefore not illegal. Neither of these contentions, however, was sustained by the Court. With respect to the first

[1] 166 U. S. 290–374 (March 22, 1897).

it said, "The language of the act includes *every* [1] contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States or with foreign nations." It therefore covers common carriers by railroad. In addressing itself to the second question the Court asked the meaning of the language in the statute stating that "every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations, is hereby declared to be illegal." The defendants argued at great length to show that Congress meant to declare illegal only those contracts that were in *unreasonable* restraint of trade. They pointed out that the common law meaning of the term "contracts in restraint of trade" included only those contracts in *unreasonable* restraint of trade, and that terms with a definite meaning at common law should be given the same meaning when used in a federal statute. "But," said the Court, "the term [contract in restraint of trade] is not of such limited signification. Contracts in restraint of trade have been known and spoken of for hundreds of years both in England and in this country, and the term includes all kinds of those contracts which in fact restrain or may restrain trade. Some of such contracts have been held void and unenforceable in the courts by reason of their restraint being unreasonable, while others have been held valid because they were not of that nature. A contract may be in restraint of trade and still be valid at common law. Although valid, it is nevertheless a contract in restraint of trade, and would be so described either at common law or elsewhere. By the simple use of the term 'contract in restraint of trade,' all contracts of that nature, whether valid or otherwise, would be included, and not alone that kind of contract which was invalid and unenforceable as being in unreasonable restraint of trade."

Again—the matter is important in view of the subsequent enunciation of the "rule of reason"—"the arguments which have been addressed to us against the inclusion of all contracts in restraint of trade, as provided for by the language of the act,

[1] The italics are the Court's.

have been based upon the alleged presumption that Congress, notwithstanding the language of the act, could not have intended to embrace all contracts, but only such contracts as were in unreasonable restraint of trade. Under these circumstances we are, therefore, asked to hold that the act of Congress excepts contracts which are not in unreasonable restraint of trade, and which only keep rates up to a reasonable price, notwithstanding the language of the act makes no such exception. In other words, we are asked to read into the act by way of judicial legislation an exception that is not placed there by the lawmaking branch of the Government, and this is to be done upon the theory that the impolicy of such legislation is so clear that it cannot be supposed Congress intended the natural import of the language it used. This we cannot and ought not to do. . . . If the act ought to read as contended for by defendants, Congress is the body to amend it and not this court, by a process of judicial legislation wholly unjustifiable." The Court then concluded that the "direct, immediate and necessary effect [of the agreement] is to put a restraint upon trade and commerce as described in the act," and it is therefore illegal.

A vigorous dissenting opinion was rendered by Justice White, and concurred in by Justices Field, Gray, and Shiras. Said Justice White, "Is it correct to say that at common law the words 'restraint of trade' had a generic signification which embraced all contracts which restrained the freedom of trade, whether reasonable or unreasonable, and, therefore, that all such contracts are within the meaning of the words 'every contract in restraint of trade'? I think a brief consideration of the history and development of the law on the subject will not only establish the inaccuracy of this proposition, but also demonstrate that the words 'restraint of trade' embrace only contracts which unreasonably restrain trade, and, therefore, that reasonable contracts, although they, in some measure, 'restrain trade,' are not within the meaning of the words."

This dissenting opinion is important, since it subsequently became the majority opinion. In the Standard Oil and the Tobacco cases Justice White (then Chief Justice) propounded

the "rule of reason," and established the principle that only contracts, etc., in unreasonable restraint of trade are forbidden by the Sherman Act.

UNITED STATES *v.* JOINT TRAFFIC ASSOCIATION [1]

This case grew out of an agreement creating an association to fix rates and fares on competitive interstate traffic east of Chicago. The agreement, to which some thirty railroads were parties, expressly declared that it was entered into only to establish and maintain reasonable rates, fares, rules, and regulations on state and interstate traffic, and that the powers conferred on the managers should not be construed to permit violation of the interstate commerce act or any other act that might be applicable. The government instituted a suit in equity to have the agreement declared void, and to enjoin its execution.

The railroads in their defense argued that the Joint Traffic Association was fundamentally different in nature from the Trans-Missouri Freight Association; that the former was not in restraint of trade at all, and was not therefore affected by the decision of the court to the effect that all restraints, reasonable and unreasonable, were illegal; that the Sherman Act, as it had been construed in the Trans-Missouri case, was unconstitutional; and that the decision in the Trans-Missouri case should be reconsidered by the Court. In none of these positions were they sustained by the Supreme Court. The Court proceeded at considerable length to state the interpretation which it had put on the Anti-trust Act. It referred to its decision in Hopkins *v.* United States, rendered on the same day.[2] "In *Hopkins v. United States* . . . we say that the statute applies only to those contracts whose direct and immediate effect is a restraint upon interstate commerce, and that to treat the act as condemning all agreements under which, as a result, the cost of conducting an interstate commercial business may be increased, would enlarge the application of the act far beyond the fair meaning of the language used. The effect upon interstate commerce must not

[1] 171 U. S. 505–578 (October 24, 1898).

[2] 171 U. S. 578–604.

be indirect or incidental only. An agreement entered into for the purpose of promoting the legitimate business of an individual or corporation, with no purpose to thereby affect or restrain interstate commerce, and which does not directly restrain such commerce, is not, as we think, covered by the act, although the agreement may indirectly and remotely affect that commerce. We also repeat what is said in the case above cited, that 'the act of Congress must have a reasonable construction, or else there would scarcely be an agreement or contract among business men that could not be said to have, indirectly or remotely, some bearing upon interstate commerce, and possibly to restrain it.' To suppose, as is assumed by counsel, that the effect of the decision in the *Trans-Missouri case* is to render illegal most business contracts or combinations, however indispensable and necessary they may be, because, as they assert, they all restrain trade in some remote and indirect degree, is to make a most violent assumption and one not called for or justified by the decision mentioned, or by any other decision of this court." [1]

The Court went on to say that the natural, direct, and immediate effect of competition is to lower rates, and thereby to increase the demand for commodities, the supplying of which increases commerce, and an agreement, whose first and direct effect is to prevent this play of competition, restrains instead of promoting trade and commerce. Inasmuch as the natural, direct, and necessary effect of the provisions of this agreement was to prevent any competition whatever between the parties to it for the whole time of its existence, it was illegal and void.

From this opinion Justices White, Gray, and Shiras dissented, but they wrote no dissenting opinion. Justice McKenna, who had succeeded Justice Field, took no part in the determination of the case. The decision, therefore, was 5–3.

ADDYSTON PIPE AND STEEL COMPANY *v.* UNITED STATES [2]

The organization and nature of the cast iron pipe pool (the Addyston Pipe and Steel Company) has already been described.[3]

[1] 171 U. S. 568. [2] 175 U. S. 211–248 (December 4, 1899). [3] See p. 12.

The government instituted proceedings against this pool, and requested the court to dissolve it and perpetually to enjoin its members from transporting cast iron pipe in interstate transportation in accordance with the provisions of the agreement. The lower court dismissed the petition,[1] but was reversed by the Circuit Court of Appeals.[2] Thereupon the Addyston Company appealed to the Supreme Court.

The defense of the Addyston Company was threefold: first, that the power of Congress to regulate interstate commerce did not include the general power to prohibit private contracts between citizens, even though such contracts resulted in a direct and substantial obstruction to or regulation of that commerce; second, that even if the combination affected interstate commerce, it was only a reasonable restraint upon a ruinous competition among themselves; and, third, that the agreement had no direct relation to interstate commerce.

The Supreme Court, in an unanimous decision, set aside all these claims. With respect to the first it held that Congress under its grant of power to regulate interstate commerce "may enact such legislation as shall declare void and prohibit the performance of any contract between individuals or corporations where the natural and direct effect of such a contract will be, when carried out, to directly, and not as a mere incident to other and innocent purposes, regulate to any substantial extent interstate commerce. . . . We do not assent to the correctness of the proposition that the constitutional guaranty of liberty to the individual to enter into private contracts limits the power of Congress and prevents it from legislating upon the subject of contracts of the class mentioned. . . . On the contrary, we think the provision regarding the liberty of the citizen is, to some extent, limited by the commerce clause of the Constitution, and that the power of Congress to regulate interstate commerce comprises the right to enact a law prohibiting the citizen from entering into those private contracts which directly and substantially, and not merely indirectly, remotely, incidentally

[1] 78 Fed. Rep. 712. [2] 85 Fed. Rep. 271.

and collaterally, regulate to a greater or less degree commerce among the States."

The second objection, that the restraint upon interstate commerce, if any, was reasonable received scant consideration at the hands of the Court. The facts as set forth in the decision of the Circuit Court of Appeals "show conclusively," it said, "that the effect of the combination was to enhance prices beyond a sum which was reasonable."

With regard to the claim of the defendants that the combination was not a direct restraint on interstate commerce the Court said: "the direct effect of the agreement or combination is to regulate interstate commerce, and the case is therefore not covered by that of *United States* v. *E. C. Knight Company*, supra. . . . The direct purpose of the combination in the *Knight case* was the control of the manufacture of sugar. There was no combination or agreement, in terms, regarding the future disposition of the manufactured article; nothing looking to a transaction in the nature of interstate commerce. . . . The case was decided upon the principle that a combination simply to control manufacture was not a violation of the act of Congress, because such a contract or combination did not directly control or affect interstate commerce, but that contracts for the sale and transportation to other States of specific articles were proper subjects for regulation because they did form part of such commerce.

"We think the case now before us involves contracts of the nature last above mentioned, not incidentally or collaterally, but as a direct and immediate result of the combination engaged in by the defendants."

This was the first decision of the Supreme Court since the Knight case that related directly to an industrial combination. Though it came too late to prevent the establishment of numerous trusts (the trust movement had already reached its crest), nevertheless it strengthened the Sherman Act, and increased the power of the government to deal with the trusts already established. In addition, it undoubtedly restrained somewhat the further creation of trusts, though it did not discourage their

formation entirely, as is shown by the fact that quite a number were organized even after the rendering of this decision.

BEMENT *v.* NATIONAL HARROW COMPANY [1]

The National Harrow Company of New Jersey owned patents on the manufacture of "float spring tooth harrows." It and Bement had entered into contracts whereunder Bement, by observing certain conditions, was licensed to manufacture and sell these implements. The conditions were, in part, that Bement would maintain the prices fixed in the license, and would not engage in the manufacture of any other type of float spring tooth harrow than that which he was authorized to manufacture. The National Harrow Company claimed that Bement had violated the contract; and it brought suit to recover damages, and to restrain the future violation thereof. The New York Court of Appeals awarded damages, whereupon an appeal was taken to the Supreme Court of the United States.

Bement in his defense argued that the contracts referred to violated the Sherman Act, and were therefore void. This, said the Court, would be a good defense, if true. The question before the Court was, therefore, did the terms of the license contracts violate the law? In endeavoring to answer this question the Court stated that the most material fact to be noted was that the agreements concerned articles protected by letters patent. The National Harrow Company was the absolute owner of the letters patent relating to the float spring tooth harrow business. "It was, therefore, the owner of a monopoly recognized by the Constitution and by the statutes of Congress. An owner of a patent has the right to sell it or to keep it; to manufacture the article himself or to license others to manufacture it; to sell such article himself or to authorize others to sell it. . . . The general rule is absolute freedom in the use or sale of rights under the patent laws of the United States. The very object of these laws is monopoly, and the rule is, with few exceptions, that any conditions which are not in their very nature illegal with regard to this kind

[1] 186 U. S. 70–95 (May 19, 1902). Justices Harlan, Gray, and White did not participate in this decision.

of property, imposed by the patentee and agreed to by the licensee for the right to manufacture or use or sell the article, will be upheld by the courts. The fact that the conditions in the contracts keep up the monopoly or fix prices does not render them illegal."

The contention had been made that the contracts did not affect interstate commerce. But, said the Court, the contracts plainly looked not only to the manufacture of these harrows in Michigan, but to their sale throughout the United States; in fact, they determined the price at which the article was to be sold throughout the country. Interstate commerce being involved, were the contracts illegal? The Court answered in the negative. "It is true," it said, "that it has been held by this court that the act included any restraint of commerce, whether reasonable or unreasonable. . . . But that statute clearly does not refer to that kind of a restraint of interstate commerce which may arise from reasonable and legal conditions imposed upon the assignee or licensee of a patent by the owner thereof, restricting the terms upon which the article may be used and the price to be demanded therefor. Such a construction of the act we have no doubt was never contemplated by its framers."

The Supreme Court threw out an implication that its decision might have been different were it established that there was a general combination among the dealers in patented harrows to regulate the sale and price of such harrows.[1] Inasmuch, however, as no such combination had been established, its decision was based on the legality of the specific contracts presented to it for its consideration.

NORTHERN SECURITIES COMPANY *v.* UNITED STATES [2]

The Northern Securities Company was incorporated in New Jersey in November, 1901, to bring under a common control the Northern Pacific Railway and the Great Northern Railway, two parallel and competing lines in the Northwest. The Northern Securities Company was to be a holding company; and it shortly acquired, by giving its own stock in exchange, more than

[1] Cf. 226 U. S. 48.

[2] 193 U. S. 197–411 (March 14, 1904).

nine-tenths of the stock of the Northern Pacific and more than three-fourths of the stock of the Great Northern. The natural effect of this arrangement undoubtedly would have been to end the competition between these two railroads; the former stockholders in the two roads, as common stockholders in the holding company, would have been interested in preventing competition, and they would have chosen as directors men who would carry out their wishes in this matter. The government, therefore, instituted a suit in equity (March 10, 1902) to have the Northern Securities Company dissolved as a combination in restraint of interstate commerce, and the railway stocks held by it returned. It charged that if this combination were not declared illegal, the efforts of the national government to preserve to the people the benefits of free competition among interstate railways would prove unavailing; in fact, that all the railroads of the country might be consolidated into one system.

The Supreme Court by a vote of 5 to 4 sustained the decree of the lower court ordering the Northern Securities Company dissolved.[1] It said, "No scheme or device could more certainly come within the words of the act—'combination in the form of a trust or otherwise . . . in restraint of commerce among the several States or with foreign nation,'—or could more effectively and certainly suppress free competition between the constituent companies. This combination is, within the meaning of the act, a 'trust'; but if not, it is a *combination in restraint of interstate and international commerce;* and that is enough to bring it under the condemnation of the act."

The Court in this connection took occasion to summarize the earlier cases arising under the anti-trust act which had received consideration at its hands. It pointed out that from these earlier decisions certain propositions bearing on the present case were plainly deducible. These propositions, stating in a nutshell the meaning of the Sherman Act as interpreted up to that time, were:

"That although the act of Congress known as the Anti-Trust

[1] The minority filed a long dissenting opinion, written in part by Justice White and in part by Justice Holmes. 193 U. S. 364–411.

Act has no reference to the mere manufacture or production of articles or commodities within the limits of the several States, it does embrace and declare to be illegal every contract, combination or conspiracy, in whatever form, of whatever nature, and whoever may be parties to it, which directly or necessarily operates *in restraint* of trade or commerce *among the several States or with foreign nations;*

"That the act is not limited to restraints of interstate and international trade or commerce that are unreasonable in their nature, but embraces *all* direct *restraints* imposed by any combination, conspiracy or monopoly upon such trade or commerce;

"That railroad carriers engaged in interstate or international trade or commerce are embraced by the act;

"That combinations even among *private* manufacturers or dealers whereby *interstate or international commerce* is restrained are equally embraced by the act;

"That Congress has the power to establish *rules* by which *interstate and international* commerce shall be governed, and, by the Anti-Trust Act, has prescribed the rule of free competition among those engaged in such commerce;

"That *every* combination or conspiracy which would extinguish competition between otherwise competing railroads engaged in *interstate trade* or *commerce*, and which would *in that way* restrain *such* trade or commerce, is made illegal by the act;

"That the natural effect of competition is to increase commerce, and an agreement whose direct effect is to prevent this play of competition restrains instead of promotes trade and commerce;

"That to vitiate a combination, such as the act of Congress condemns, it need not be shown that the combination, in fact, results or will result in a total suppression of trade or in a complete monopoly, but it is only essential to show that by its necessary operation it tends to restrain interstate or international trade or commerce or tends to create a monopoly in such trade or commerce and to deprive the public of the advantages that flow from free competition;

"That the constitutional guarantee of liberty of contract does

not prevent Congress from prescribing the rule of free competition for those engaged in *interstate and international* commerce." [1]

The recognition of these principles, said the Court, must lead us to grant the relief asked for by the government unless the special objections raised by the defendants to the application of the Sherman Act to the present case are substantial. These objections in part were: the Northern Securities Company was a state corporation authorized to acquire stock, and the enforcement of the Sherman Act against it would be an unauthorized interference by the national government with the internal commerce of the states creating it and its subsidiary railway companies; that so far as the power of Congress was concerned, citizens or state corporations might dispose of their property and invest their money in any way they chose; and that the enforcement of the act would lead to business disaster, and widespread financial ruin. All these objections were considered and dismissed by the Court. The Anti-trust Act, it said, has been construed as forbidding any combination which by its necessary operation destroys or restricts free competition among those engaged in interstate commerce; in other words, that to destroy or restrict free competition in interstate commerce was to restrain such commerce. Simply because a state allows consolidation, it does not follow that the stockholders of two or more state railroad corporations, having competing lines and engaged in interstate commerce, could lawfully combine and form a distinct corporation to hold the stock of the constituent corporations, and, by destroying competition between them, in violation of the act of Congress, restrain commerce among the states and with foreign nations. "No State can, by merely creating a corporation, or in any other mode, project its authority into other States, and across the continent, so as to prevent Congress from exerting the power it possesses under the Constitution over interstate and international commerce, or so as to exempt its corporation engaged in interstate commerce from obedience to any rule lawfully established by Congress for such commerce. . . . Every corporation created by a State is nec-

[1] 193 U. S. 331–332. Italics are the Court's.

essarily subject to the supreme law of the land; . . ." and "the court may make any order necessary to bring about the dissolution or suppression of an illegal combination that restrains interstate commerce. . . ." The affirmance of the judgment below will mean that no device, "however skilfully such device may have been contrived, and no combination, by whomsoever formed, is beyond the reach of the supreme law of the land, if such device or combination by its operation directly restrains commerce among the States or with foreign nations in violation of the act of Congress."

The Supreme Court therefore sustained the decree of the lower court. The Northern Securities Company was enjoined from voting the stock of the Northern Pacific Railway Company and the Great Northern Railway Company, and the railroad companies were enjoined from paying any dividends on such stock to the Northern Securities Company. But the Northern Securities Company might return to the Northern Pacific and the Great Northern, respectively, the stock of these roads held by it; or it might transfer the stocks of these railroad companies to its own shareholders.[1]

This decision was of capital importance in the interpretation of the Sherman Act, since it was the first instance in which a holding company was attacked as a combination in restraint of trade. But it was of equal importance in its influence upon economic conditions. It gave a decided set-back to the use of the holding company device in the organization of trusts; and it greatly encouraged the federal government in instituting proceedings against them.

SWIFT AND COMPANY *v.* UNITED STATES [2]

This was a bill in equity against Swift and Company, Armour and Company, Cudahy Packing Company, Nelson Morris and Company, Schwarzchild and Sulzberger, Hammond Packing

[1] For a later decision of the Supreme Court approving the plan of dissolution agreed upon, see Harriman *v.* Northern Securities Company, 197 U. S. 244–299.

[2] 196 U. S. 375–402 (January 30, 1905).

Company, and G. H. Hammond Company, controlling about 60 per cent of the total trade in fresh meats.[1] The bill charged a combination of a dominant proportion of the packers throughout the United States not to bid against each other in the live stock markets of the different states, except perfunctorily and without good faith, thus securing the live stock at less than competitive prices; a combination to bid up prices for a few days in order to induce the cattle men to send their stock to the stockyards; to fix the prices at which they would sell to dealers throughout the states, these prices being effected by secret periodical meetings and maintained by a restriction of shipments, by the establishment of a uniform rule for the giving of credit, and by the keeping of a black list of delinquents; a combination to make uniform and improper charges for cartage; and, finally, to get less than lawful rates from the railroads to the exclusion of shippers. It was further charged that because of the consequent inability of competitors to continue in commerce, the defendants had monopolized the commerce in live stock and fresh meats among the states. The government prayed for an injunction of the most comprehensive sort. The Circuit Court upheld the government; and issued an injunction restraining the defendants from entering into a combination, in violation of the Sherman Act, and from employing any of the aforesaid devices, or any other method or device, the purpose or effect of which was to restrain commerce.[2] The defendants thereupon appealed to the Supreme Court, but without success. The Court unanimously held that an illegal combination had been shown; and that the effect of the combination on interstate commerce was direct, and not accidental, secondary, or remote. The case was to be distinguished from United States *v.* E. C. Knight Company. In the Knight case the subject-matter of the combination was manufacture, and the direct object was monopoly within a state. However likely it was that monopoly of commerce among the states in sugar would follow from the agreement entered into, such was not a necessary

[1] Petition in United States *v.* Swift and Company, pp. 1, 4.

[2] The injunction is quoted in 196 U. S. 393.

consequence, nor a primary end. But in this case the subject-matter was sales, and the very point of the combination was to restrain and monopolize commerce among the states in respect of such sales. The Supreme Court therefore affirmed the injunction, except that it ordered the elimination therefrom of the words "or by any other method or device, the purpose and effect of which is to restrain commerce as aforesaid." The specific devices mentioned in the bill stood prohibited, but the Court felt that it would be quite unjust to issue a general injunction against all possible breaches of the law, since that would put the whole conduct of the defendant's business at the peril of a summons for contempt.

LOEWE *v.* LAWLOR [1]

Mr. Loewe, a manufacturer of hats at Danbury, Connecticut, and engaged in interstate commerce in the sale of his hats, operated an open shop. The United Hatters of North America, a labor organization, forming a part of the American Federation of Labor, demanded that Mr. Loewe employ union labor exclusively, that is, convert his plant into a closed shop. Upon his refusal the United Hatters went on strike, and instituted a boycott against the hats manufactured by Mr. Loewe. Finding it difficult to dispose of his product in interstate commerce, Mr. Loewe brought an action against Mr. Lawlor and the United Hatters of North America for the recovery of three-fold damages under section seven of the Sherman Act.

The question before the Court was whether upon the facts averred and admitted an action could be maintained. The Court in an unanimous decision held that it could. The Sherman Act, it said, "prohibits any combination whatever to secure action which essentially obstructs the free flow of commerce between the States, or restricts, in that regard, the liberty of a trader to engage in business," and the combination described was in restraint of trade or commerce among the several states in the sense in which those words were used in the act. The

[1] 208 U. S. 274–309 (February 3, 1908).

Supreme Court therefore remanded the cause to the lower court to determine the truth of the facts alleged and the amount of the damages to be awarded.

THE STANDARD OIL COMPANY OF NEW JERSEY ET AL. *v.* THE UNITED STATES [1]

The government brought suit on November 15, 1906, against the Standard Oil Company of New Jersey (the holding company), seventy subsidiary corporations, and seven individual defendants, charging violation of the Sherman Act. The Circuit Court in an unanimous decision on November 20, 1909, held that the Standard Oil Company was a combination in restraint of trade in violation of section one and a monopoly in violation of section two of the anti-trust act, but it ordered the bill against thirty-three of the corporate defendants dismissed, since it had not been proven that they were engaged in the operation of the combination. The Circuit Court thereupon issued a decree,[2] which provided (substantially in the Court's language):

Section 5. That the Standard Oil Company, its directors, officers, agents, servants, and employees, are enjoined from voting any of the stock in any of the thirty-seven companies named in section two of the decree, and from exercising or attempting to exercise any control or influence over the acts of these subsidiary companies by virtue of its holding of their stock. And the subsidiary companies, their officers, etc., are enjoined from paying any dividends to the Standard Oil Company of New Jersey, and from permitting the latter to vote any stock in, or direct the policy of any of them. "But the defendants are not prohibited by this decree from *distributing ratably to the shareholders of the principal company* the shares to which they are equitably entitled in the stocks of the defendant corporations that are parties to the combination." [3]

Section 6. That the defendants named in section two of the decree, their officers, etc., are enjoined from continuing the com-

[1] 221 U. S. 1–106 (May 15, 1911). [2] 173 Fed. Rep. 197–200.
[3] Italics supplied by the author.

bination adjudged illegal, and from entering into any like combination or conspiracy, the effect of which is, or will be, to restrain commerce in petroleum or its products among the States, etc., or to prolong the unlawful monopoly of such commerce possessed by defendants, either (1) by the use of liquidating certificates; by placing the control of any of said corporations in a trustee; by causing its stock or property to be held by others than its equitable owners; or by any similar device; or (2) by making any express or implied agreement together, like that adjudged illegal, relative to the control or management of any of said corporations, or the price or terms of purchase, or of sale, or the rates of transportation, of petroleum or its products in interstate or international commerce, or relative to the quantities thereof purchased, sold, transported, or manufactured by any of said corporations, which will have a like effect in restraint of commerce to that of the combination the operation of which is hereby enjoined.

Section 7. The defendants named in section two are enjoined, until the discontinuance of the operation of the illegal combination, from engaging in interstate commerce.

Section 9. This decree shall take effect thirty days after its entry if no appeal is taken from it; and if an appeal is taken, it shall take effect, unless reversed or modified, within thirty days after the final decision of the Supreme Court upon appeal.

The Standard Oil Company of New Jersey, thirty-three of the thirty-seven other corporate defendants, and the seven individual defendants at once appealed to the Supreme Court. The case was argued before the Court in March, 1910, but on account of the illness of Justice Moody, and the death of Justice Brewer in the latter part of March, the case was reargued in January, 1911. The decision of the Court was rendered on May 15, 1911.

The Supreme Court in approaching the problem raised by the case pointed out that the views of the two parties to the suit as to the meaning of the Sherman Act and as to the facts were as "wide apart as the poles." But since both agreed that the controversy in its every aspect was controlled by a correct

conception of the meaning of sections one and two of the Sherman Act, the Court proposed to consider first of all the text of these sections of the act, and its meaning in the light of the common law and the law of the country at the time of its adoption.

The first section of the Sherman Act deals with restraint of trade, and the second with attempts to monopolize, and monopolization. The Court, guided by the principle that words which had a well-known meaning at common law or in the law of this country were presumed to have been used in that sense in a statute unless the context compelled to the contrary, reviewed briefly certain indisputable propositions already established by the English and American law prior to the enactment of the Sherman Act. It then concluded with respect to the first section: That the context manifests that the statute was drawn in the light of the existing practical conception of the law of restraint of trade; that in view of the many new forms of contracts and combinations which were being evolved from existing economic conditions it was deemed essential by an all-embracing enumeration to make sure that no form of contract or combination by which an undue restraint of interstate or foreign commerce was brought about could save such restraint from condemnation; that the statute under this view evidenced the intent not to restrain the right to make contracts, whether resulting from combination or otherwise, which did not unduly restrain interstate or foreign commerce; that as the contracts or acts embraced in the provision were not expressly defined, it inevitably followed that the provision necessarily called for the exercise of judgment, which required that some standard should be resorted to for the purpose of determining whether the prohibitions contained in the statute had or had not in any given case been violated; that, thus not specifying, but indubitably contemplating and requiring a standard, it was intended that the *standard of reason*[1] which had been applied at the common law and in this country in dealing with subjects of the character embraced by the statute, was intended to be the

[1] Italics supplied by the author.

measure used for the purpose of determining whether in a given case a particular act had or had not brought about the wrong against which the statute provided.

With respect to the second section a consideration of the text served to establish, said the Court, that this section was intended to supplement the first, and to make sure that by no possible guise could the public policy embodied in the first section be frustrated or evaded. The words "to monopolize" reach every act bringing about the prohibited results. The ambiguity, if any, is involved in determining what is intended by monopolize. But this ambiguity is readily dispelled, said the Court, in the light of the previous history of the law of restraint of trade to which we have referred, and the indication which it gives of the practical evolution by which monopoly and the acts which produce the same result as monopoly, that is, an undue restraint of the course of trade, all came to be spoken of as restraint of trade. In other words, having by the first section forbidden all means of monopolizing trade, that is, unduly restraining it by means of every contract, combination, etc., the second section seeks, if possible, to make the prohibitions of the act all the more complete and perfect by embracing all attempts to reach the end prohibited by the first section, that is, restraints of trade, by any attempt to monopolize, even though the acts by which such results are attempted to be brought about be not embraced within the general enumeration of the first section. And, of course, when the second section is thus harmonized with and made, as it was intended to be, the complement of the first, it becomes obvious that the criterion to be resorted to in any given case for the purpose of ascertaining whether violations of the section have been committed, is the *rule of reason* [1] guided by the established law and by the plain duty to enforce the prohibitions of the act, and thus the public policy which its restrictions were obviously enacted to subserve.

While the meaning of sections one and two thus seemed clear to the Court, it proposed, before applying its interpretation, to consider the contentions of the plaintiff and defendants, which

[1] Italics supplied by the author.

would give a different significance to the act than that adopted by the Court.

The fundamental contention of the government was that the language of the statute embraced every contract, combination, etc., in restraint of trade, and hence left no room for judgment. It held further that this was the interpretation that had been placed upon the act by the Court, notably in the freight association cases. In reply the Court said that it was undoubtedly true that in the opinion in each of the freight association cases general language was made use of, which, when separated from its context, would justify the conclusion that it was decided that reason could not be resorted to for the purpose of determining whether the acts complained of were within the statute. Yet it was also true that the nature and character of the contract or agreement in each case was fully referred to, and suggestions as to their unreasonableness pointed out, in order to indicate that they were within the prohibitions of the statute. That the cases relied upon did not, when rightly construed, sustain the doctrine contended for was established, it held, by all of the numerous decisions of this court which have applied and enforced the anti-trust act, since they all in the very nature of things rest upon the premise that reason was the guide by which the provisions of the act were in every case interpreted. Indeed in Hopkins *v.* United States, decided after the Trans-Missouri Freight Association case, but before the Joint Traffic Association case, the Court said, "to treat as condemned by the act all agreements under which, as a result, the cost of conducting an interstate commercial business may be increased would enlarge the application of the act far beyond the fair meaning of the language used. There must be some direct and immediate effect upon interstate commerce in order to come within the act." And "if the criterion by which it is to be determined in all cases whether every contract, combination, etc., is a restraint of trade within the intendment of the law, is the direct or indirect effect of the acts involved, then of course the rule of reason becomes the guide, and the construction which we have given the statute, instead of being refuted by the cases relied upon, is by

those cases demonstrated to be correct." In other words, the rule of reason and the result of the test as to direct and indirect in their ultimate aspect come to one and the same thing. But "in order not in the slightest degree to be wanting in frankness, we say that in so far, however, as by separating the general language used in the opinions in the *Freight Association* and *Joint Traffic cases* from the context and the subject and parties with which the cases were concerned, it may be conceived that the language referred to conflicts with the construction which we give the statute, they are necessarily now limited and qualified."[1]

The contentions of the defendants were fundamentally: first, that the act could not be constitutionally applied to the case before the court, since this would result in extending the power of Congress over mere questions of production within the states; and, second, that the act could not be applied without impairing rights of property and destroying the freedom of contract or trade, which were protected by the constitutional guaranty of due process of law. The first contention, said the Court, is foreclosed by the numerous decisions since the Knight case; and the second assumes that reason may not be resorted to in applying the statute, and that therefore the right to contract is unreasonably restricted. But since we have pointed out that reason may be resorted to, the proposition based on an unsound assumption falls to the ground.

The meaning of the Sherman Act having been set forth, what was the status under this act of the Standard Oil Company? The established facts, said the Court, demonstrate the illegality of the combination before us; the Standard Oil Company is not only a combination in restraint of trade, but a combination in *unreasonable* restraint of trade. It turned next, therefore, to a consideration of the remedy to be applied.

Ordinarily, said the Court, adequate relief against acts done in violation of the statute would result from restraining the doing of such acts in the future. But in a case like this where there exists not only a continued attempt to monopolize, but also a monopolization, the duty to enforce the statute requires the

[1] 221 U. S. 67–68.

application of broader remedies. The essential remedies are: first, to forbid the doing in the future of acts violative of the statute; and, second, the exertion of such measure of relief as will effectually dissolve the illegal combination. The Court then proceeded as a means of determining the relief to be granted to consider the relief afforded by the Circuit Court. The decree of the Circuit Court is given on page 406, and need not be repeated here. The Supreme Court affirmed this decree of the lower court except in certain particulars. It held, first, that the interests involved were so vast that the defendants should be allowed six months to carry out the decree, instead of only thirty days. Second, it thought that section seven of the decree, forbidding interstate commerce to the New Jersey corporation and its subsidiary companies until the dissolution of the combination, might work serious injury to the public, and should not have been awarded. And, finally, the Supreme Court construed section six of the decree as restraining the stockholders or the corporations, after the dissolution of the combination, from, by any device whatever, recreating, directly or indirectly, the illegal combination, but not as depriving them of the power to make normal and lawful contracts or agreements. For example, after the dissolution some of the separate pipe-line companies might desire to combine so as to form a continuous line. Such action, the Court held, would not be repugnant to the act, yet it might be deemed to have been restrained by the decree of the court below. Section six was therefore modified to permit such lawful arrangements. As thus modified the decree was affirmed, and the court below was allowed to retain jurisdiction to the extent necessary to compel compliance in every respect with its decree.[1]

The decision that the Standard Oil Company was unlawful was a unanimous one, but Justice Harlan filed a separate opinion dissenting from certain parts of the decision, particularly the enunciation of the "rule of reason." Relentlessly he cited from

[1] The decree of the Circuit Court, modified to meet the views of the Supreme Court, was filed July 29, 1911; and may be found in Decrees and Judgments in Federal Anti-Trust Cases, pp. 136-144.

former decisions of the Court, particularly the Trans-Missouri Freight case and the Joint Traffic case, passages indicating that the Court had substantially modified its former position.[1] The Court, said Justice Harlan, now says to those who object to all legislative prohibition of contracts, combinations, and trusts in restraint of interstate commerce, "you may *now* restrain such commerce, provided you are reasonable about it; only take care that the restraint is not undue." [2] As the result of this upsetting of the long-settled interpretation of the act we will doubtless have, he said, in cases without number, the constantly recurring inquiry—*difficult to solve by proof*[3]—whether the particular contract, combination, or trust involved in each case is or is not an "unreasonable" or "undue" restraint of trade. But more dangerous in his opinion was the fact that the decision of the Court in this case represented judicial legislation,—a usurpation of the constitutional functions of the legislative branch of the government. Justice Harlan held that the Court had done in this case exactly what in the Trans-Missouri Freight case it had refused to do; that in the Trans-Missouri Freight case the Court had held that the act prohibited every contract, etc., in restraint of trade, and that to read into the act the word "unreasonable" would be an act of judicial legislation; and this they could not and ought not to do. The Supreme Court, therefore, by interpretation of a statute has changed, he said, the public policy adopted by Congress,—a proceeding that might well cause some alarm for the integrity of our institutions.[4]

UNITED STATES *v.* AMERICAN TOBACCO COMPANY; AMERICAN TOBACCO COMPANY *v.* UNITED STATES [5]

The suit against the tobacco trust was brought on July 10, 1907. The defendants were twenty-nine individuals, sixty-five

[1] In speaking of the Standard Oil and the Tobacco cases Judge Peter Grosscup said, "It would be mere hypocrisy to say that the court has not turned upon itself. What the court fourteen years ago said was not in the act the court now say *is* in the act." (North American Review, 194, p. 3.)

[2] Italics are Justice Harlan's.

[3] Italics supplied by the author.

[4] 221 U. S. 83, 105.

[5] Ibid., 106–193 (May 29, 1911.)

American corporations, and two English corporations. For convenience the corporate defendants were classified by the upper court as follows: the American Tobacco Company (a corporation organized in New Jersey in 1904 to merge the properties formerly controlled through the Consolidated Tobacco Company, a holding company) was called the primary defendant; the American Snuff Company, the American Cigar Company, the American Stogie Company, the MacAndrews and Forbes Company, and the Conley Foil Company were called the accessory defendants; the remaining fifty-nine American corporations, the subsidiary defendants; and the Imperial Tobacco Company and the British-American Tobacco Company, the English corporations. The bill charged that the defendants, individual and corporate, constituted a combination in restraint of interstate and foreign trade in tobacco in violation of section one of the Sherman Act, and a monopolization of such trade in violation of section two. The decision of the Circuit Court, rendered on November 7, 1908, was favorable to the government, though one of the four judges dissented.[1] The decree of the Court was filed on December 15, 1908.[2] Inasmuch as the Supreme Court in subsequently awarding its decree did not model its action upon that of the Circuit Court, the decree of the lower court need not be outlined here. It suffices to say that the Circuit Court dismissed the petition as to the individual defendants, the English corporations, the United Cigar Stores Company, and three other of the subsidiary corporations, but granted relief with respect to the remaining defendants. From the decree both parties appealed to the Supreme Court, the government because the petition had been dismissed in part and because the decree awarded did not satisfy it, and the defendants because the petition had not been dismissed as to all of the defendants. The decision of the Supreme Court was rendered on May 29, 1911, the pronouncement being delayed by the same causes that made a reargument of the Standard Oil case advisable.

The Supreme Court found its task much simplified by the analysis and review of the act made in the Standard Oil case.

[1] 164 Fed. Rep. 700–728. [2] 164 Fed. Rep. 1024–1025.

Its investigation in the tobacco case proceeded along three lines: first, a review of the undisputed facts; second, the construction and application of the act; and, third, the remedy to be applied. The facts as to the tobacco trust are found in Chapter VII, and we may therefore proceed at once to the second branch of the Court's inquiry, the interpretation of the Sherman Act.

The Court pointed out first of all the significance of the case before it. It said, "If the Anti-trust Act is applicable to the entire situation here presented and is adequate to afford complete relief for the evils which the United States insists that situation presents it can only be because that law will be given a more comprehensive application than has been affixed to it in any previous decision. This will be the case because the undisputed facts as we have stated them involve questions as to the operation of the Anti-trust Act not hitherto presented in any case." It then pointed out why this was so. Even if the ownership of stock by the American Tobacco Company in the accessory and subsidiary companies and the ownership of stock in any of these companies among themselves were held, as in the Standard Oil case, to be a violation of the act, the question would remain whether the American Tobacco Company, and the five accessory defendants, by virtue of the power that remained to them, would still be in existence in violation of the Sherman Act. Again, the question would remain whether those companies whose power arose, not from combination, but from the acquisition and ownership of property, were amenable to the prohibitions of the act. Further, the question would remain whether certain companies no longer in themselves a restraint of trade or a monopolization, when once they had been bereft of the power resulting from stock ownership, should nevertheless be restrained because of their intimate connection with other defendants.

The Court then proceeded to apply the act as formerly interpreted to the case before it. By the interpretation which we have put on the act, said the Court, all the difficulties suggested by the form in which the assailed transactions are clothed become of no moment. This follows because the first and second

sections of the Sherman law, when taken together, embrace every conceivable act which could possibly come within the spirit or purpose of the prohibitions of the law, without regard to the garb in which such acts are clothed; that is to say, the public policy which that statute manifests can not be frustrated by resort to any disguise or subterfuge of form.

Considering, then, the undisputed facts, it only remains, said the Court, to determine whether they establish that the acts, contracts, agreements, and combinations which were assailed were of such a wrongful character as to bring them within the prohibitions of the law. That they were, the undisputed facts made abundantly clear. The wrongful purpose and the illegality of the tobacco combination is overwhelmingly established, said by the Court, by the following considerations: a. By the fact that the very first organization or combination was impelled by a previously existing fierce trade war, evidently inspired by one or more of the minds which brought about and became parties to that combination. b. Because, immediately after that combination, the acts which ensued justify the inference that the intention existed to use the power of the combination as a vantage ground to further monopolize the trade in tobacco by means of trade conflicts designed to injure others, either by driving competitors out of the business or compelling them to become parties to a combination—a purpose whose execution was illustrated by the plug war, by the snuff war, and by the conflict which immediately followed the entry of the combination into England and the division of the world's business by the two foreign contracts which ensued. c. By the ever-present manifestation which is exhibited of a conscious wrongdoing by the form in which the various transactions were embodied from the beginning, ever changing but ever in substance the same. d. By the gradual absorption of control over all the elements essential to the successful manufacture of tobacco products, and by placing such control in the hands of seemingly independent corporations serving as perpetual barriers to the entry of others into the tobacco trade. e. By persistent expenditure of millions upon millions of dollars in buying out plants, not for the purpose of

utilizing them, but in order to close them up and render them useless for the purposes of trade. f. By the constantly recurring stipulations, by which numbers of persons, whether manufacturers, stockholders, or employees, were required to bind themselves, generally for long periods, not to compete in the future. "Indeed, when the results of the undisputed proof which we have stated are fully apprehended, and the wrongful acts which they exhibit are considered, there comes inevitably to the mind the conviction that it was the danger which it was deemed would arise to individual liberty and the public well-being from acts like those which this record exhibits, which led the legislative mind to conceive and to enact the Anti-trust Act, considerations which also serve to clearly demonstrate that the combination here assailed is within the law as to leave no doubt that it is our plain duty to apply its prohibitions."

The application of remedies involves greater difficulties, held the Court, than any case interpreting the Anti-trust Act hitherto decided. This is true, first, because a mere decree forbidding stock ownership by one part of the combination in another part would not afford adequate relief, since there would still remain different ingredients of the combination, still able, by the character of their organization, to continue the wrongful situation. Second, because the subtle devices resorted to were of such a character as to make it difficult, if not impossible, to restore in their entirety the original lawful conditions. Third, because the affair was so involved that there was danger of injuring the public, and possibly of perpetuating the illegal condition. The Court said that it might at once issue a permanent injunction restraining the combination as a universality and all the individuals and corporations which formed a part of it from continuing to engage in interstate commerce until the illegal situation was cured, or it might direct the appointment of a receiver to take charge of the assets of the combination to prevent a continued violation of the law, and to work out by a sale of the property of the combination a condition not repugnant to the act. But it did not order either of these remedies. To stay the interstate transportation by defendants of tobacco

and its products might inflict infinite injury on the public by leading to the stoppage of supply and a great enhancement of prices; and the resort to a receivership might not only do grievous injury to the public, but also cause widespread loss to many innocent people. It, therefore, having held that the petition should not have been dismissed against the individual defendants, the United Cigar Stores Company, and the foreign corporations, decreed as follows: (1) That the combination in and of itself, as well as each and all of the elements composing it, whether corporate or individual, whether considered collectively or separately, be decreed to be in restraint of trade and an attempt to monopolize and a monopolization. (2) That the court below, in order to give effective force to our decree, be directed to hear the parties for the purpose of determining upon some plan of dissolving the combination and of recreating, out of the elements now composing it, a new condition which shall be honestly in harmony with and not repugnant to the law. (3) That for the accomplishment of these purposes a period of six months is allowed, with leave, however, to the court below to extend such period to a further time not to exceed sixty days. (4) That in the event, before the expiration of the period thus fixed, a condition of disintegration in harmony with the law is not brought about, it shall be the duty of the court, either by way of an injunction restraining the movement of the products of the combination in the channels of interstate or foreign commerce or by the appointment of a receiver, to give effect to the requirements of the statute. Meanwhile the defendants should be restrained from doing any act which might enlarge the power of the combination.[1]

Justice Harlan, as in the Standard Oil case, assented in part and dissented in part. He agreed most thoroughly that the American Tobacco Company and its parts should be decreed to be in restraint of interstate trade and a monopolization. But he objected to sending the case back to the Circuit Court in order that a new condition might be "recreated" that would not be in violation of the law; there was enough evidence in the record, he said, to enable the Supreme Court to formulate specific direc-

[1] For an account of the final plan of dissolution, see pp. 452 seq.

tions as to what the decree should contain. He objected also to the reaffirmance of the "rule of reason." "Congress, with full and exclusive power over the whole subject, has signified its purpose to forbid *every* restraint of interstate trade, in whatever form, or to whatever extent, but the court has assumed to insert in the act, by construction merely, words which make Congress say that it means only to prohibit the 'undue' restraint of trade. If I do not misapprehend the opinion just delivered, the court insists that what was said in the opinion in the *Standard Oil Case*, was in accordance with our previous decisions in the *Trans-Missouri* and *Joint Traffic cases*, . . . if we resort to *reason*. This statement surprises me quite as much as would a statement that black was white or white was black. . . . By every conceivable form of expression, the majority, in the *Trans-Missouri* and *Joint Traffic cases*, adjudged that the act of Congress did not allow restraint of interstate trade to any extent or in any form, and three times it expressly rejected the theory, which had been persistently advanced, that the act should be construed as if it had in it the word 'unreasonable' or 'undue.' But now the court, in accordance with what it denominates the 'rule of reason,' in effect inserts in the act the word 'undue,' which means the same as 'unreasonable,' and thereby makes Congress say what it did not say, what, as I think, it plainly did not intend to say and what, since the passage of the act, it has explicitly refused to say. It has steadily refused to amend the act so as to tolerate a restraint of interstate commerce even where such restraint could be said to be 'reasonable' or 'due.' In short, the court now, by judicial legislation, in effect amends an act of Congress relating to a subject over which that department of the Government has exclusive cognizance."

HENRY *v.* A. B. DICK COMPANY [1]

The facts in this case were briefly as follows: The A. B. Dick Company owned the patent on a stencil-duplicating machine

[1] 224 U. S. 1–73 (March 11, 1912). This case was decided under the patent law rather than under the anti-trust law, but its bearing on the trust problem is sufficient to justify its inclusion.

known as the "Rotary Mimeograph." The company sold one of these machines to a Miss Skou under a license restriction attached to the machine, which stated that the machine was sold by the Dick Company with the license restriction that it might be used only with the stencil paper, ink, and other supplies made by the Dick Company. The defendant, Sidney Henry, a dealer in ink, sold to Miss Skou for use on the machine a can of ink not made by the Dick Company; and this with knowledge of the license restriction and with the expectation that it would be used in connection with the mimeograph. The Dick Company brought suit against Henry, alleging that the patent on the mimeograph had been infringed by the breach of the conditions upon which the patented machine was sold; and sought an injunction against indirect infringement by Henry.

The Court rendered a judgment in favor of the Dick Company. The patent laws, the Court pointed out, grant to the inventor the exclusive right to make, use, and sell the invention; and each of these is a separable right. Thus, one person may be permitted to make, but not to sell or use, the patented article. Another may be permitted to sell, but within a limited area, or for a particular use. A third may be permitted only to use the patented article. While an absolute and unconditional sale of a patented article operates to place it beyond the boundaries of the patent, and thus places the purchaser in possession of the article to do with as he pleases, the owner of the patent, under his right to exclusive use of the patented article, may pass the property right to a purchaser under license restrictions which will give him the right to use the machine only for specified purposes or at specified places. This is because a patent monopoly gives the separate rights of manufacture, sale, and use. When, therefore, a patentee makes and sells a patented device, the extent of the license to use, which is carried by the sale, depends on whether any restriction was placed on its use, and brought home to the person acquiring the article. The Court held that it was clear from the license restriction adopted in this case that while the property in the machine passed to the purchaser, the sale carried with it only the right to use the invention according to the terms of the

license; and among these terms was the use of ink made by the Dick Company.

The Court then turned to an examination of the nature of the restrictions that might be lawfully imposed on a purchaser of a patented article. It declared that it would construe the patent law as granting a monopoly in order to subserve a broad public policy,—the encouragement of invention. It referred with approval to the Bement case.[1] In that case it was held that a contract in regard to the use of a patent, even though it restrained interstate trade, did not fall within the prohibitions of the Sherman Act, if it involved only the reasonable and legal conditions imposed under the patent law. But, it was argued, to permit the seller to restrict the buyer to a use of the mimeographing machine in connection with ink made by the patentee would give the latter the power to extend his monopoly so as to embrace articles not within the patent. To cite one of the suggestions pressed upon the Court, it was said that a patentee of a coffee pot might sell on the condition that the pot be used only with coffee bought from him. While granting that competition in the sale of ink, coffee, etc., might be slightly affected by such restrictions, the Court held that these illustrations failed to show marked inconvenience to the public, since the public was always free to take or refuse the patented article on the terms imposed. If the terms were too onerous, the patented article would not find a market; and the public, by permitting the invention to go unused, lost nothing which it had before. When the patent expired the public would be permitted to use the invention without compensation or restriction. "It must not be forgotten," said the Court, "that we are dealing with a constitutional and statutory monopoly. . . . We are not at liberty to say that the Constitution has unwisely provided for granting a monopolistic right to inventors, or that Congress has unwisely failed to impose limitations upon the inventor's exclusive right of use. And if it be that the ingenuity of patentees in devising ways in which to reap the benefit of their discoveries requires to be restrained, Congress alone has the power to determine what restraints shall

[1] See p. 398.

be imposed." (In 1914, as a part of the anti-trust legislation of that year, Congress acted upon this suggestion; and in section three of the Clayton Act specifically forbade such restrictive sales as the Supreme Court had upheld in the Dick case). [1]

From the opinion in the Dick case Chief Justice White and Justices Hughes and Lamar dissented. Inasmuch as the case was argued after the death of Justice Harlan and during the absence of Justice Day, the decision was 4 to 3.

Subsequently—after the passage of the Clayton Act—the Supreme Court in the Motion Picture Patents Company case said: "Under the patent law the grant by patent of the exclusive right to use, like the grant of the exclusive right to vend, is limited to the invention described in the claims of the patent, and that law does not empower the patent owner by notices attached to the things patented to extend the scope of the patent monopoly by restricting their use to materials necessary for their operation but forming no part of the patented invention, or to send such articles forth into the channels of trade subject to conditions as to use or royalty, to be imposed thereafter, in the vendor's discretion." [2] By this decision Henry *v.* Dick was definitely overruled.

UNITED STATES *v.* ST. LOUIS TERMINAL ASSOCIATION [3]

This case is significant since it illustrates the "advantages" that may result from the adoption of the Court's "rule of reason." It was the first case in which the Court held that a combination which was illegal because in unreasonable restraint of trade might, by a modification of its provisions, become a lawful combination. The decision was unanimous, although Justice Holmes did not participate in the hearing of the case.

The geographical and topographical conditions at St. Louis are unusual. On the east lies the Mississippi river, which constitutes quite an obstacle to railroad communications. The cost of constructing a bridge over the river is so great that the railroads have not endeavored to build their own bridges, but

[1] Cf. p. 361.

[2] 243 U. S. 502 (April 9, 1917).

[3] 224 U. S. 383–413 (April 22, 1912).

each has made use of a toll bridge,—open to all railroads. From the west access to the city is almost as difficult. The city is located on hills which approach close to the river bank, and it was found necessary to tunnel these hills in order to connect the city with the valley of Mill creek, where the roads from the west had their termini. Gradually the Terminal Railroad Association of St. Louis acquired the several independent terminal companies which ministered to the needs of different groups of railroads, until finally it was practically impossible for any railroad to pass through, or even enter, St. Louis without using the facilities controlled by this company.

The question before the Court was whether this unification of the terminal facilities was a combination in restraint of trade within the meaning of the Sherman Act. The Court held that the mere combining of several independent terminal systems into one was not necessarily a restraint upon interstate commerce; a unified terminal system open to all on equal terms might be of the greatest public utility, particularly in a city like St. Louis. The question was whether this particular terminal association was unreasonable. The Court held that it was. In the first place, the association was controlled by fourteen of the twenty-four railroads which converged at St. Louis, while the other ten had no stock interest in it. And no railroad might become a member of the terminal association without the unanimous consent of the fourteen proprietary companies, as they were called. While counsel for the terminal company claimed that no company which applied would be refused joint use or ownership of the terminal company, the fact was that the requirement of unanimous consent still remained. It was also true that the terminal company paid no dividends, and disclaimed any intention of ever paying any; and that the non-proprietary railroads were permitted to use the facilities of the terminal company upon paying the same charges as were paid by the proprietary companies. But, said the Court, there is no provision guaranteeing them this privilege. It may also be true, said the Court, that the proprietary companies have not availed themselves of the full measure of their power to impede the free competition

of outside companies, yet it objected to the fact that the companies outside the terminal association were under compulsion to use the terminal system, yet had no voice in its control. The Court therefore found the terminal company to be an unreasonable restraint of interstate commerce.

The government had asked for the dissolution of the terminal company and the apportionment of its business among the three leading component parts. As matters had stood prior to the enunciation of the rule of reason, it is likely that the petition of the government would have been granted. But the Court now held that if the terminal association were to become the *bona fide* agent of every railroad that used its facilities it would no longer be an illegal restraint of trade, and that by this means there would be preserved for the public the obvious advantages of unification, thus vindicating the wise purpose of the statute.

STANDARD SANITARY MANUFACTURING COMPANY *v.* UNITED STATES [1]

This was a suit brought by the government against sixteen corporate and thirty-four individual defendants. The corporate defendants were manufacturers of sanitary enameled iron ware, such as bath tubs, wash bowls, drinking fountains, sinks, and closets. Up to about 1910 they were in competition with each other, but the government alleged that they had then established a combination controlling 85 per cent of the country's output of enameled iron ware.

The process of enameling consisted in sifting enameling powder upon iron ware brought to a red heat. The high temperature fused the powder, and there was thus formed on the utensil a hard, impenetrable, insoluble, and smooth surface. There were a number of patents covering the application of the powder, but the best one was owned by the Standard Sanitary Manufacturing Company, which manufactured some 50 per cent of the enameled iron ware. For some time this company refused to license any other manufacturer to use its invention, but

[1] 226 U. S. 20–52 (November 18, 1912).

finally it seems to have become convinced that the market for its products was being damaged through the production of inferior ware under other patents. Accordingly it was agreed that this company, and the Mott Iron Works, and L. Wolff Manufacturing Company, owners of the other leading patents, would for a nominal consideration assign their patents to one Mr. Wayman, secretary of an association of enameled ware manufacturers, subject to re-assignment after two years upon demand by the owner of the patent. Mr. Wayman was then to license the various manufacturers to use these patents. The form of the license agreements was determined by a committee, and in the summer of 1910 sixteen manufacturers of enameled iron ware signed license agreement papers.

The license agreements entered into by the manufacturers provided that the licensee (the manufacturer) might use the patents held by Mr. Wayman by paying a royalty of $5.00 per day for each furnace operated. The agreements established a scale of prices which the licensee agreed to maintain; and contained provisions whereunder changes in prices might be made from time to time. Manufacturers complying with the agreements were to receive back at the end of each month 80 per cent of the royalties paid by them.

In addition, the jobbers were brought into the combination. The jobbers agreed to maintain the resale prices as fixed from time to time, and not to handle the goods of non-licensed manufacturers, except upon the written permission of the licensor. A breach of any of the conditions of the agreement subjected the contract and all unfilled orders to cancellation, involved a forfeiture of the rebates that the jobbers received for complying with the agreement, and further a forfeiture of the power to obtain from licensed manufacturers any ware manufactured under the patents.

The government claimed that this scheme was an attempt to conceal an agreement fixing prices under the guise of a licensing arrangement for the use of patents; that behind the "grinning mask" of the license agreement was the common, vulgar type of monopoly which had many times been condemned by the Court

as dangerous alike to individual liberty and public well-being.[1] The defendants denied these allegations, and relied in large measure on the privileges accorded by the patent laws.

The Court in an unanimous opinion said: "The agreements clearly . . . transcended what was necessary to protect the use of the patent or the monopoly which the law conferred upon it. They passed to the purpose and accomplished a restraint of trade condemned by the Sherman law. It had, therefore, a purpose and accomplished a result not *shown*[2] in the *Bement Case*. . . . Rights conferred by patents are indeed very definite and extensive, but they do not give any more than other rights an universal license against positive prohibitions. The Sherman law is a limitation of rights, rights which may be pushed to evil consequences and therefore restrained."

UNITED STATES *v.* READING COMPANY; TEMPLE IRON COMPANY *v.* UNITED STATES; READING COMPANY *v.* UNITED STATES[3]

This was a bill in equity filed by the government to dissolve the anthracite coal combination.[4] The original defendants in the suit may be divided into three groups: (1) the Reading Company (a holding company); (2) the Philadelphia and Reading Railway and five other anthracite railroads; and (3) the respective coal companies of the railroads, including the Temple Iron Company, jointly owned by the six defendant carriers. The Government claimed that there existed between the defendants a *general combination* formed to restrain competition in the production, sale, and transportation in interstate commerce of anthracite coal. It contended that this general combination was established: first, by evidence of an agreement among the carrier defendants to apportion among themselves according to a scale of percentages the total output of coal transported from

[1] 226 U. S. 29–30.

[2] Italics supplied by the author.

[3] 220 U. S. 324–373 (December 16, 1912). Justices Day, Hughes, and Pitney took no part in this decision.

[4] For a detailed account of this combination see the author's "The Anthracite Coal Combination in the United States."

the mines to tidewater; second, by a combination, through the instrumentality of the Temple Iron Company, to prevent the construction of a new and competing line to tidewater; third, by a combination to buy, according to a series of identical contracts, the coal produced by the independent operators, thus preventing competition between the coal produced by the defendants and that produced by the independents; and, fourth, by certain contributory combinations, participated in by certain of the defendants, including the purchase by the Erie of the New York, Susquehanna and Western and of the Pennsylvania Coal Company (with its allied railroads), and the acquisition by the Reading Company of a majority of the stock of the Central Railroad of New Jersey.

"The case," said the Court, "is barren of *documentary* evidence of solidarity," [1] and therefore the fact of a general combination, if it exists, must be deduced from specific acts or transactions in which the companies have united, and from which a general combination may be inferred. The first charge was that the general combination was established by the agreement entered into between the carriers in 1896 to distribute, according to a definite scale of percentages, the tonnage of anthracite shipped from the coal regions to New York Harbor. The Court pointed out that the limited character of the coal field invited such agreements, and that it was probable that there was a conference in 1896 as charged; but it held that the scheme, if attempted (which was not proven), had been abandoned long before the bill was filed, and that the government had therefore failed to show any contract or agreement for the distribution of tonnage.

The second step in the carrying out of the illegal combination was alleged to be the combination of six anthracite carriers through the Temple Iron Company to prevent the construction of the New York, Wyoming and Western Railroad,—a proposed independent line to tide-water.[2] Through the Temple Iron

[1] 226 U. S. 344. Italics supplied by the author.

[2] For details see the author's The Anthracite Coal Combination in the United States, pp. 74–82.

Company, owned by the six defendant carriers, the collieries of the principal supporters of the new road were purchased, and the New York, Wyoming and Western, to use the Court's language, was "successfully strangled." This combination the Court held to be illegal. It pointed out that the Temple Iron Company "has been and still is an efficient agency for the collective activities of the defendant carriers for the purpose of preventing competition in the transportation and sale of coal in other States. . . . Through it, the defendants, in combination, may absorb the remaining output of independent producers." The Court held that the board of directors of the Temple Iron Company, "composed as it is of men representing the defendants, supplies time, place and occasion for the expression of plans or combinations requiring or inviting concert of action."

The third charge was that the defendants and a number of the independent operators had entered into contracts, containing substantially uniform provisions agreed upon beforehand by the defendant carriers in concert, whereby the independents agreed to deliver to the railroad coal company with which the contract was negotiated all the coal *thereafter* mined by them in return for a definite percentage of the average selling price of coal at tidewater points at or near New York City.[1] It was further charged that the price paid was more than the operator could get if he attempted to market his coal independently, and that the difference was the sum paid for the privilege of controlling the sale of the independent output.

The Supreme Court sustained these charges of the government, and declared the percentage contracts illegal. It recited the persistent attempts of the coal operators not connected with the railroads to gain an independent outlet to tidewater,—attempts which offered a constant menace to the monopoly of transportation enjoyed by the defendants. The obvious solution from the standpoint of the defendants was to tie up the independent operators by means of perpetual contracts for

[1] For the details as to these "percentage" contracts see the author's "The Anthracite Coal Combination in the United States," pp. 87–97.

the sale of their coal. The Court said that it was not surprised that the railroads were willing to offer unusually favorable terms, as the perpetual contracts would remove forever the inducement to the entry of competing lines of anthracite carriers, and would remove, also, the coal of the independents from competition with the coal of the defendants. To suppress competition through the percentage contracts would require, however, concerted action, as the attempt of a few to secure the independent coal would have been resisted by the others. The Court held that the defendants had thus acted in concert, and that the contracts were therefore unlawful, even though singly they might not have been in restraint of trade.

The final charge was that the purchase of the New York, Susquehanna and Western and the Pennsylvania Coal Company by the Erie, and of the Central of New Jersey by the Reading Company, were illegal. This charge was dismissed by the Court. It held that it did not appear from the record that any one of these three transactions was the result of any general combination between all of the defendants, and if they did not constitute any part of a general plan or combination entered into by all the carrier companies, their separate consideration as independent violations of the law was not admissible under the general frame of the bill. As to the legality of these three minor combinations the Court expressed no opinion, but directed that the bill, in so far as it sought relief against them, be dismissed, without prejudice to the bringing of a new action.

UNITED STATES *v.* PATTEN [1]

This was a criminal prosecution brought against Mr. James A. Patten, charging violation of the Sherman Act through the establishment of a corner in cotton. It presented the question, to use the Court's language, whether a conspiracy to run a corner in the available supply of a staple commodity, such as cotton, normally a subject of trade and commerce among the states, and thereby to enhance artificially its price throughout the country, was within the terms of section one of the Anti-trust

[1] 226 U. S. 525–544 (January 6, 1913).

Act. The Circuit Court had held that it was not, and for three reasons: first, that the conspiracy did not belong to the class in which the members, engaged in interstate trade, agreed to suppress competition among themselves.[1] But the Supreme Court held that section one, on which the counts were founded, related not solely to voluntary restraints, such as resulted when persons engaged in interstate trade agreed to suppress competition among themselves, but related as well to involuntary restraints, such as resulted when persons not so engaged conspired to compel action by others, or to create artificial conditions, which necessarily impeded or burdened the due course of such trade or restricted the common liberty to engage therein.

The Circuit Court had held, second, that running a corner, instead of restraining competition, tended, temporarily at least, to stimulate it. With respect to this point the Supreme Court said, "It may well be that running a corner tends for a time to stimulate competition; but this does not prevent it from being a forbidden restraint, for it also operates to thwart the usual operation of the laws of supply and demand, to withdraw the commodity from the normal current of trade, to enhance the price artificially, to hamper users and consumers in satisfying their needs, and to produce practically the same evils as does the suppression of competition."

Third, the Circuit Court had held that the obstruction of interstate trade resulting from the operation of the conspiracy, even although a necessary result, would be so indirect as not to be a restraint in the sense of the statute. The Supreme Court in analyzing this claim outlined the salient features of the conspiracy. It was, it said, a conspiracy to run a corner in the market. The commodity to be cornered was cotton, a product of the southern states, mainly used in the northern states, and therefore necessarily the subject of interstate commerce. The corner was to be conducted on the Cotton Exchange in New York City, but by means that would enable the conspirators to obtain control of the available supply, and to enhance the price to all buyers in every market of the country. Upon the corner

[1] 188 Fed. Rep. 664–673.

becoming effective, there could be no trading in the commodity save at the will of the conspirators, and at such price as their interests might prompt them to exact. The conspiracy was thus to bring within its dominating influence the entire cotton trade of the country. Such being the nature, object, and scope of the conspiracy it was plain that by its necessary operation it would directly and materially impede the due course of commerce among the states, and therefore inflict upon the public the injuries which the Anti-trust Act was designed to prevent.[1]

UNITED STATES *v.* WINSLOW [2]

This was a criminal proceeding brought against the president of the United Shoe Machinery Company and others, charging them with forming a combination in restraint of trade and with forming a conspiracy. The alleged facts were substantially as follows: Practically all the shoes worn in the United States are made with the aid of lasting machines, welt-sewing machines, outsole-stitching machines, heeling machines, and metallic-fastening machines. Up to February 7, 1899, the Consolidated and McKay Lasting Machine Company made 60 per cent of the lasting machines; the Goodyear Shoe Machinery Company made 80 per cent of the welt-sewing and outsole-stitching machines, and 10 per cent of the lasting machines; and the McKay Shoe Machinery Company made 70 per cent of the heeling machines, and 80 per cent of the metallic-fastening machines. On February 7, 1899, these three companies organized the United Shoe Machinery Company to unite the businesses formerly separately controlled. The organization of the United Shoe Machinery Company and its acquisition of the stocks and business of these companies was alleged to constitute a breach of the Sherman Act.

The opinion of the Court was unanimous and brief, being embraced in less than four pages. It is to be observed, said the Court, that the conditions now inserted in the leases of shoe

[1] From this opinion Chief Justice White and Justices Lurton and Holmes dissented.

[2] 227 U. S. 202–218 (February 3, 1913).

machinery to shoe manufacturers are not alleged to have been contemporaneous with the combination, or to have been contemplated when it was made. The District Court construed the indictment as confined to the combination of February 7 without regard to the leases subsequently made, and we have no jurisdiction to review this interpretation of the indictment. The validity of the leases or of a combination contemplating them is therefore not before us.

The question to be decided, said the Court, is whether the combination taken by itself was within the penalties of the Sherman Act. Thus limited the question did not require much discussion. On the face of it the combination was merely an attempt to secure greater efficiency. The business of the several companies that combined, as it existed prior to the combination, is assumed to have been legal. The machines are patented, making them a monopoly in any event; and it may be assumed that the success of the several companies was due to their patents having been the best. As, by the interpretation of the lower court and by the admission in argument before us, these companies did not compete with one another, it is difficult to see why the collective business should be any worse than its component parts. We can see no greater objection to one corporation manufacturing seventy per cent of three noncompeting groups of patented machines collectively used for making a single product than to three corporations making the same proportion of one group each. The disintegration aimed at by the statute does not extend to reducing all manufacture to isolated units of the lowest degree. The case was therefore dismissed.

UNITED STATES *v.* UNITED SHOE MACHINERY COMPANY [1]

The government instituted suit against the United Shoe Machinery Company on December 12, 1911. It charged a combination of manufacturers of shoe machinery, and it specifically attacked certain leases of the company which were asserted to be the means whereby competition in the manufacture

[1] 247 U. S. 32–91 (May 20, 1918).

of shoe machinery was restrained.[1] The defendant claimed that it had merely combined noncompeting businesses; and that the leases were but the exercise of undoubted patent rights. The District Court dismissed the bill, whereupon the government appealed to the Supreme Court.[2] This body in an opinion rendered on May 20, 1918, upheld the decision of the lower court by a vote of four to three (Justices McReynolds and Brandeis, having been connected with suits against the company, being debarred by professional ethics from participation in the case).

The charge of the government was two-fold: first, that the United Company had effected a combination of competing concerns engaged in the manufacture of shoe machinery in violation of sections one and two of the Sherman Act; and, second, that it had entered into leases with shoe manufacturers which extended the control achieved by the act of combination. With respect to the first contention the Supreme Court held that the companies that united to form the United Shoe Machinery Company were complementary, not competitive. It admitted that the testimony was conflicting, and might lead to a different conclusion; but it accepted the verdict of the lower court that there was no practical competition among these companies. It decided likewise as to the companies acquired after the organization of the combination in 1899. These acquisitions, it held, did not remove competition "in any practical or large sense."

Under this interpretation there was obviously no occasion to dissolve the United Shoe Machinery Company. It was undoubtedly a trust, since it represented the union of a group of concerns monopolizing various branches of the shoe machinery business. But it was not an illegal trust, since the constituent companies were patent monopolies, protected by law; and since, not being competitive with each other, there was no bar to their combination.

With respect to the leases and their tying clauses the Court held that they were simply the exercise of the company's right as a patentee. The leases perhaps restrained the trade of com-

[1] For an account of the United Shoe Machinery Company, see ch. 8.

[2] 222 Fed. Rep. 349–415.

peting manufacturers of shoe machinery, but this was of the nature of a patent. The very strength of a patent consists in the right it gives to exclude others from the use of the invention or to permit them to use it on terms imposed by the patentee; and its employment in this manner was not necessarily an offense against the Anti-trust Act. The Court pointed out that the patents did not permit unlawful restraints, such as were employed by the Standard Sanitary Manufacturing Company; but the leases of the United Shoe Machinery Company were not of that nature. They were bargains based on patent rights, agreed to by the lessees, and entitled to the sanction of the law.

In a dissenting opinion (concurred in by Justices Day and Pitney) Justice Clarke declared that some of the companies originally combined in the United Company were competitive; that this was established by the testimony of the organizers. These individuals, knowing precisely what they hoped to accomplish, had rejected a "harmonious arrangement" or a "working agreement" from an idea that "it might be deemed to be a combination in restraint of trade," but to accomplish the same end had adopted the scheme of merger, later condemned by the Supreme Court in the Tobacco case as a mere subterfuge of form. Justice Clarke vigorously protested against deciding the case upon refined distinctions as to the application of the patent law.

In a separate dissenting opinion (concurred in by Justices Clarke and Pitney) Justice Day attacked particularly the majority opinion sustaining the tying clauses in the leases. Referring to Straus *v.* American Publishers' Association, in which the Court had held that the patent statute was not intended to authorize agreements in unlawful restraint of trade and tending to monopoly, in violation of the specific terms of the Sherman law,[1] he declared that it was apparent from a mere statement of the terms of the lease restrictions that they tended to monopolize an important trade in interstate commerce. To sustain the provisions of the leases he regarded as a grant of authority to holders of patented inventions to build up monopolies in direct

[1] 231 U. S. 234.

violation of the Sherman Act, under the guise of leasing the use of patented machinery.

UNITED STATES *v.* INTERNATIONAL HARVESTER COMPANY [1]

The organization of the harvester trust has been described in chapter X. In 1912 the government instituted suit under the Sherman Act, asking for the dissolution of the company. The Circuit Court decided in favor of the government on August 12, 1914. The company appealed to the Supreme Court, but before a decision was rendered it withdrew its appeal, and accepted the decree of the lower court. The nature of the dissolution agreed upon will be described in chapter XVIII; at this point merely the decision of the Circuit Court will be outlined.

The Circuit Court, Judge Sanborn dissenting, held the International Harvester Company to be a combination in unreasonable restraint of trade. Three separate opinions were rendered. Judge Smith, after reviewing the facts and pertinent decisions, said that while there was no limit under the American law to which a business might not independently grow, and while even a combination of two or more companies was not illegal if it did not unreasonably restrain trade, yet when 80 to 85 per cent of the business was combined, and by the combination all competition was eliminated between the members thereof, the resulting restraint of trade was unreasonable. He therefore ordered the harvester trust dissolved.

Judge Hook concurred in the foregoing opinion. He said in part: "The International Harvester Company is not the result of the normal growth of the fair enterprise of an individual, a partnership or a corporation. On the contrary, it was created by combining five great competing companies which controlled more than 80 per cent. of the trade in necessary farm implements, and it still maintains a substantial dominance. That is the controlling fact; all else is detail."

Judge Sanborn dissented at considerable length. He dissented because in his opinion the crucial issue was not whether in 1902 the International Harvester Company had established a combi-

[1] 214 Fed. Rep. 987–1012.

nation in restraint of trade, but whether in 1912, when the suit was brought, it was then unreasonably restraining or monopolizing trade, or threatening to do so; and because the evidence in the case had convinced him that the company was not then and had not for at least seven years previous to the commencement of the suit been restraining or threatening to restrain trade unduly. The criterion of "unreasonable" restraint he held to be a restriction of competition that unduly injured the public by (1) raising the prices of the articles, or (2) limiting their production, or (3) deteriorating their quality, or (4) decreasing the prices paid for the labor or materials required to produce them, or (5) oppressing competitors; and the evidence established, he maintained, that the company had not been guilty of any of these practices. He therefore favored the dismissal of the suit without prejudicing the right of the government to institute similar proceedings whenever the company committed any acts in violation of the Sherman law.

The Harvester case was thus a highly significant one, since it clearly presented to the courts the question whether the Sherman Act forbids combinations that hold a dominant or preponderant position in the industry, entirely apart from the manner in which they exercise their vast power; or whether it merely forbids such combinations when they abuse their power, as, for example, by advancing prices, limiting the supply, lowering the quality, reducing wages, or oppressing competitors. To state it somewhat differently, the Harvester case involved a determination of the question whether the Sherman Act forbids all trusts, or merely the "bad" trusts; for the International Harvester Company was a "good" trust, if there were any such. It is therefore much to be regretted that through the force of circumstances a decision of the Supreme Court on this vital matter was not obtained.

UNITED STATES *v.* CORN PRODUCTS REFINING COMPANY [1]

On March 1, 1913, the government filed a petition against the Corn Products Refining Company, asking that it be adjudged

[1] 234 Fed. Rep. 964–1018. A study of the glucose trust is in Dewing, Corporate Promotions and Reorganizations, ch. 4.

to be a combination in restraint of trade and an illegal monopoly. The decision of the District Court sustaining the government, and granting the relief prayed for, was rendered on June 24, 1916. The company appealed, but subsequently withdrew its appeal. The decision of the lower court was thus controlling.

With regard to the law the Court, referring to the Harvester case, agreed that it was an open question whether the test of illegality under the Sherman Act was to be found only in the combination of enough producing capacity to control supply and fix prices, or whether it must also be proven that the combination had used its power to the injury of the public; but it expressed the opinion that the test was the power, and not its exercise. In the case of the Corn Products Refining Company, however, this question was held to be academic, since the company was illegal under either test. The company by the combination in 1906 had acquired control of all the glucose plants in the country, and of plants making about 64 per cent of the output of starch; and had manifested a "continuous and deliberate purpose . . . by every device which their ingenuity could discover, to maintain as completely as possible their original domination of the industry." It thus had the power—diminished, to be sure, since 1906, yet still the power—to restrain trade; and it had steadfastly used it in an illegal manner.

The issue was therefore as to the remedy. The necessity of an injunction to restrain the company from employing in the future those unfair practices that had hampered independent enterprise in the past was held to be clear; and the court therefore specifically forbade the resort to low-price campaigns, bogus independents, price agreements, and the like. As to the advisability of a dissolution the Court was not so certain, but it decided, in view of the "inveterate and incorrigible" insistence of the company upon interfering with freedom of commerce, to prescribe also the more drastic remedy. The Court did not indicate what the form of the decree would be—the plan was to be filed with the Federal Trade Commission, as permitted by the Trade Commission Act—but it stated that it would be similar to the

Harvester decree, and it implied that no dissolution would be satisfactory that left as much as 60 per cent of the trade in the hands of one company.[1]

UNITED STATES *v.* UNITED STATES STEEL CORPORATION [2]

The organization of the United States Steel Corporation has been discussed in chapter IX. In October, 1911, the government brought suit against the company, asking that it be dissolved on the ground that it was engaged in an illegal restraint of trade, and was a monopoly. In a decision rendered on June 3, 1915, the District Court judges unanimously dismissed the bill, though they disagreed as to the grounds for the dismissal.[3] The decision of the Supreme Court came on March 1, 1920. Four judges found for the Steel Corporation, three against, and two did not participate, one having as Attorney General been associated with the proceeding against the Corporation, and the other as a private citizen having expressed the opinion that the Corporation was illegal and uneconomic. It is probable, therefore, as in the Shoe Machinery case, that the decision of the Court did not represent the opinion of the majority.

The Supreme Court after reviewing the decisions of the judges of the lower court held that it was clear that while there might be two opinions as to the purpose of the organizers of the Steel Corporation, there was no doubt that the Corporation had never possessed, and did not then possess, a monopoly. And it was against monopoly that the Sherman Act was directed; not against the expectation thereof, but against its realization. The Corporation, to be sure, had attained much greater power than any other competitor, yet not greater than all of them combined; and monopoly therefore had not been achieved.[4] Because of its failure to achieve monopoly the Corporation had found it advisable to coöperate with its competitors through pools, associations, trade meetings, and social dinners. The Court held these

[1] The substance of the decree is given on p. 484.

[2] 251 U. S. 417–466 (March 1, 1920).

[3] 223 Fed. Rep. 55–179.

[4] 251 U. S. 444.

arrangements to be violations of the law, yet transient in their purpose and effect. From a conviction of their futility they had been abandoned nine months before the suit was brought; and they had not been resumed, nor was there any evidence of an intention to resume them. Even the government did not anticipate their resumption, said the Court, for it failed to avail itself of the offer of the lower court to retain jurisdiction of the case for the purpose of enjoining such acts, if they were ever attempted.

The Corporation not having a monopoly, what could be charged against it? It had not the power unaided to fix prices; and it had not committed any acts of aggression upon its competitors. It was of impressive size, to be sure, yet the law, the Court held, does not make mere size nor the existence of unexerted power an offense; rather it requires the performance of overt acts. When there were no restraints of competitors in the trade nor any complaints by customers, it was difficult to see, said the Court, how there could be any restraint of trade.

In conclusion the Court found itself unable to discover how the public interest would be subserved by the dissolution of the Corporation; on the contrary, its dissolution might do injury to the public interest, including a material disturbance to the foreign trade. The bill of the government was accordingly dismissed.

The dissenting opinion held that the record left no fair room for doubt that the Steel Corporation and its several subsidiary corporations were formed in violation of the Sherman Act. It quoted with approval from the opinion of Judge Woolley of the lower court, who found that the control of the various steel companies later combined in the Corporation had embraced in some instances from 80 to 95 per cent of the total output of the country, and had resulted in an immediate increase in prices, in some cases double and in other cases treble what they had been before, yielding in consequence large dividends upon greatly inflated capital. It was held that the record disclosed that the Corporation for many years after its formation had exerted its power to control and maintain prices by pools, associations,

trade meetings, and dinners; and that in combination with its competitors it had an ability "to fix prices and restrain the free flow of commerce upon a scale heretofore unapproached in the history of corporate organization in this country."

The dissenting opinion agreed that the Sherman Act offers no objection to the size that a corporation may reach, nor to the continued exertion of lawful power, when that size and power were obtained by lawful means and developed by natural growth. But it declared that the reiterated decisions of the Supreme Court had held that this power might not legally be derived from conspiracies, combinations, or contracts in restraint of trade; and that to hold otherwise was practically to annul the Sherman Act by judicial decree.

Concluding the dissenting opinion Justice Day held that the decision of the majority amounted to an assertion that the Steel Corporation and its subsidiaries, although organized in plain violation and bold defiance of the Sherman Act, nevertheless were immune from a decree effectually ending the combinations, because of some reasons of public policy requiring such conclusion. But, he said, "I know of no public policy which sanctions a violation of the law, nor of any inconvenience to trade, domestic or foreign, which should have the effect of placing combinations, which have been able to thus organize one of the greatest industries of the country in defiance of law, in an impregnable position above the control of the law forbidding such combinations. Such a conclusion does violence to the policy which the law was intended to enforce, runs counter to the decisions of the court, and necessarily results in a practical nullification of the Act itself."

CHAPTER XVIII

TRUST DISSOLUTION PROCEEDINGS

In this chapter the record of the several administrations in the enforcement of the anti-trust laws will be summarized, the trust dissolution proceedings will be described at some length, and the results will be briefly appraised.

During the administration of Benjamin Harrison, who was President at the time of the passage of the Sherman Act (1890), four bills in equity and three indictments were brought under the anti-trust act.[1] The first important case was U. S. *v.* Greenhut,[2] a criminal indictment of the officers of the Distilling and Cattle Feeding Company (the whisky trust) for an alleged monopolization of the manufacture and sale of distilled spirits. The district judge in quashing the indictment said that the indictment averred merely that the defendants had monopolized the manufacture and sale of distilled spirits, and did not aver that they had monopolized, or combined to monopolize, interstate or foreign commerce in distilled spirits. The indictment therefore charged no offense within the letter or spirit of section two of the Sherman Act.

The outcome of this suit may be interpreted as a severe counter indictment of the Department of Justice; and it is perhaps indicative of the attitude of this department that it allowed itself to be discouraged by this rebuff, and decided to abandon altogether the prosecution of the whisky trust.

Another case was U. S. *v.* Patterson,[3] a criminal proceeding

[1] The Federal Antitrust Laws, July 1, 1916, pp. 44–46. This pamphlet contains a list of the cases instituted by the United States under the anti-trust acts.

[2] 50 Fed. Rep. 469 (May 16, 1892).

[3] 55 Fed. Rep. 605 (February 28, 1893); and 59 Fed. Rep. 280 (June 1, 1893).

against the members of a combination to control the price of cash registers. The indictment was sustained in part by a lower court, but the Attorney General allowed the case to lapse because the complaining witness had joined the combination.[1] This was indeed a strange outcome of a case brought under a law designed to prevent combinations in restraint of trade.

A more important case was U. S. *v.* E. C. Knight Company, a bill in equity to prevent the American Sugar Refining Company (the sugar trust) from retaining control of the four Philadelphia refineries, the acquisition of which, it was alleged, constituted a violation of the Sherman Act. The government lost this suit, as already pointed out,[2] because of defects in procedure. It attacked the defendants for acts relating to the business of sugar refining *within* a state, and failed to produce any proofs of a restraint upon interstate commerce. Had the government under the direction of the Attorney General presented its cause properly the decision of the Supreme Court in this case—the first one involving the Sherman Act to come before it—would probably have been different, and the trust movement of the late nineties might never have taken place.

None of the other four cases instituted during President Harrison's administration were trust cases. One was a freight association case (the Trans-Missouri Freight Association); another was a trade union case; and the other two dealt with combinations more or less local in character.[3] It is clear, therefore, that the trust cases initiated during President Harrison's administration came to naught, and that this was largely owing to the attitude of the first two Attorney Generals, whose official duty it was to enforce the statute.

During the second term of President Cleveland (1893–1897) there were brought four bills in equity, two indictments, and two contempt proceedings.[4] The most important of these cases was U. S. *v.* Addyston Pipe and Steel Company, a bill in equity

[1] The Federal Antitrust Laws, July 1, 1916, p. 46.

[2] See p. 388.

[3] The Federal Antitrust Laws, July 1, 1916, pp. 44–46.

[4] Ibid., pp. 46–49.

to dissolve the cast iron pipe combination.[1] The government obtained a victory in this instance,—a victory which doubtless restrained somewhat the subsequent activities of trust promoters, since it demonstrated that the Sherman Act was really possessed of "teeth." Yet this case was the only one of the eight that dealt with an industrial combination of national importance. Four of them dealt with trade unions, one with a traffic association (the Joint Traffic Association), and the other two with organizations of rather limited scope. It may be asked why no proceedings were instituted against the cigarette, oil, powder, cordage, and other trusts, all of which were more important than the cast iron pipe combination, which, after all, was essentially a pool, and therefore in some ways not so dangerous as the more binding organizations left undisturbed by the Attorney General. No doubt the Department of Justice was discouraged by the decision in the Knight case, and no doubt the funds available for investigation and prosecution were limited;[2] yet this hardly explains the failure to prosecute the trusts, against which the law was really aimed, rather than such organizations as the Kansas City Live Stock Exchange.

If the accomplishments of the Harrison and Cleveland administrations were meagre, those of the McKinley administration were even more so. During the four and a half years of McKinley's presidency no criminal prosecutions were brought and only three bills in equity.[3] Of these three, one was against a local live stock association, another against a combination of coal dealers in California, and the third against a combination of coal producers in Ohio and West Virginia. It was during this administration that the modern trust movement reached its height, and yet not a single suit against a trust was brought.

Upon the death of President McKinley on September 14, 1901, Theodore Roosevelt became President. In marked contrast to his predecessor in office, President Roosevelt enforced

[1] For the decision of the Supreme Court, see p. 395.

[2] See Annual Report of the Attorney General (Harmon) for 1896, p. XXVII.

[3] The Federal Antitrust Laws, July 1, 1916, pp. 49–50.

the Sherman Anti-trust Act with decided vigor. During the seven and one-half years of his administration there were brought eighteen bills in equity, twenty-five indictments, and one forfeiture proceeding.[1] Among the trusts attacked were the oil trust (the Standard Oil Company), the tobacco trust (the American Tobacco Company), and the powder trust (the du Pont de Nemours and Company). Lesser combinations attacked included those in the meat-packing, salt, paper, licorice, elevator, naval stores, and furniture industries. Moreover, a number of important railroad combinations were proceeded against. These included the Northern Securities Company, the St. Louis Terminal Railroad Association, the Reading Company, the Union Pacific Railroad Company, and the New Haven Railroad Company. Furthermore, legislation was enacted to create a Bureau of Corporations; to expedite cases arising under the anti-trust act; and to supply the Department of Justice with ample funds to prosecute unlawful combinations.

The record of the Roosevelt administration in turn was far eclipsed by that of the Taft administration. During the seven and one-half years of Roosevelt's presidency forty-four proceedings all told had been instituted, while during the four years that Taft was President there were brought forty-six bills in equity, forty-three indictments, and one contempt proceeding,—a total of ninety, or more than twice as many proceedings in about half as long a period.[2] Moreover, the suits filed by Attorney General Wickersham (President Taft's Attorney General) included a number of very important trusts and combinations not disturbed by the preceding administration. Among them were the following: the United States Steel Corporation, the American Sugar Refining Company, the United Shoe Machinery Company, the International Harvester Company, the National Cash Register Company, the Keystone Watch Case Company, the Corn Products Refining Company, the Standard Sanitary Manufacturing Company, the American Thread Company, the General Electric Company, and the American Coal Products Company.

[1] The Federal Antitrust Laws, July 1, 1916, pp. 50–61.

[2] Ibid., pp. 61–81.

During President Wilson's first term thirteen bills in equity and twenty-one indictments were filed, a total of thirty-four as compared with ninety during the four years of his predecessor.[1] Furthermore, far-reaching amendments to the Sherman Act were enacted. During the period down to September 8, 1920, twenty-two additional bills and twenty-four additional indictments were brought. Among the combinations proceeded against were: the Eastman Kodak Company, the Quaker Oats Company, the American Can Company, the Lehigh Valley Railroad, and (for the second time) the Reading Company and the New Haven Railroad. The list is not imposing, yet by the beginning of President Wilson's administration the principal trusts and combinations had already been proceeded against.

The individual dissolution proceedings may next be described.

THE OIL TRUST

The first trust to be formally dissolved under the Sherman Act was the Standard Oil Company.[2] The history of the suit against this company and the decrees of the Circuit and Supreme Courts have already been outlined. The reader will recall that the decree of the Circuit Court—which was approved in the main by the Supreme Court—forbade the Standard Oil Company of New Jersey, and its officers and directors, to vote the stock of its subsidiary companies; to exercise any control over their operations; to continue the unlawful combination; or to enter into any like combination to restrain commerce. But the Court specifically said that the Standard Oil Company of New Jersey was not prohibited by the decree from distributing ratably to its shareholders the shares of stock in the subsidiary companies parties to the combination to which they (the share-

[1] See Annual Reports of the Attorney General.

[2] A paper combination was dissolved by judicial order on May 11, 1906, but this combination, brought about by making the General Paper Company the sales agent for some twenty-three paper concerns, was essentially a pool. (See Report of the Senate Committee on Control of Corporations, 1913, p. 945.) A combination of elevator companies, including the Otis Elevator Company, was dissolved by a decree entered June 1, 1906, but this was a consent decree. (See ibid., p. 946.)

holders) were equitably entitled. This suggestion was seized upon by the defendants, and made the basis of their plan of dissolution. In a circular dated July 28, 1911, the Standard Oil Company of New Jersey (the parent company) announced that it would distribute to its stockholders (as of September 1, 1911) the stock of thirty-two American subsidiaries and of one foreign subsidiary; and this distribution was made on December 1.[1] By this distribution each owner of one share of stock in the Standard Oil Company of New Jersey received securities (generally fractional shares) of an aggregate face value of approximately $178; [2] and in addition retained, of course, his stock in the parent company, which continued as a producing concern, operating its large refineries at Bayonne, New Jersey; Baltimore, Maryland; and Parkersburg, West Virginia.

The decree contained no express prohibition of common officers or directors among the New Jersey corporation and its former subsidiaries (none of which was dissolved), but at meetings of the Standard Oil Company of New Jersey and the Standard Oil Company of New York on December 4 some important changes in organization were made. Mr. John D. Rockfeller resigned as president and director of the Standard Oil Company of New Jersey. Mr. William Rockefeller, president of the Standard Oil Company of New York, vice president of the Standard Oil Company of New Jersey, and a director in both companies, resigned from all these positions. Mr. John D. Archbold, vice president of the Standard Oil Company of New Jersey, was elevated to the presidency; but resigned as vice president and director of the Standard Oil Company of New York. Mr. H. C. Folger, Jr., vice president of the New York concern, was made president; but he handed in his resignation as secretary and director of the New Jersey company. Mr. A. C. Bedford, a director of the New York concern, resigned to become vice president and treasurer of the New Jersey concern.

[1] The stock of the foreign subsidiary was not distributed until a later date.

[2] The value of the shares of the subsidiaries was computed by the Commercial and Financial Chronicle, and the results presented in the form of a table. See vol. 93, p. 1390 (November 18, 1911).

(Upon the death of Mr. Archbold some years later Mr. Bedford became president.) Similar shifts affecting other positions were made at the same time.

What has been the effect of the dissolution decree? Fortunately the Federal Trade Commission, which was empowered by the Trade Commission Act to investigate the manner in which the dissolution decrees of the courts have been carried out, has made a full investigation of this matter so far as gasoline is concerned. Its findings of fact and its conclusions are contained in its *Report on the Price of Gasoline in 1915*.

The conclusion of the Commission was that in spite of the dissolution decree there was little, if any, competition among the former subsidiaries of the Standard Oil Company of New Jersey in the marketing of gasoline, now the chief refined product of crude oil.[1] The subsidiaries which were engaged in marketing gasoline were the Standard Oil companies of New York, New Jersey, Kentucky, Ohio, Indiana, Nebraska, California, and Louisiana, the Atlantic Refining Company, the Continental Oil Company, and the Magnolia Petroleum Company. The Commission pointed out that these eleven Standard companies have with respect to gasoline "maintained a complete division of territory embracing the whole country and that almost without exception each Standard marketing company occupies and supplies a distinct and arbitrarily bounded territory."[2] Thus, the Standard Oil Company of New York occupied the whole of New York state and the New England states, but no other territory; the Atlantic Refining Company occupied all of Pennsylvania and Delaware, but no part of any other state; and the Standard Oil Company of New Jersey served New Jersey, Maryland, Virginia, West Virginia, North Carolina, and South Carolina.[3] The only exceptions to this division of territory without any overlapping were found in Oklahoma and Arkansas. In

[1] Report of the Federal Trade Commission on Price of Gasoline in 1915, pp. 7, 113.

[2] Ibid., p. 6.

[3] The details are shown in a map opposite page 22 of the Report of the Commission.

Oklahoma—the territory of the Magnolia Petroleum Company —the Standard Oil Company of Indiana had a few tank wagon stations in the northern part of the state; and in Arkansas both the Magnolia Petroleum Company and the Standard Oil Company of Louisiana had stations. None of the "independent" concerns, it should be observed, had marketing territories limited in this fashion. The Texas Company, for example, sold gasoline in 32 states and the District of Columbia, and covered ten of the eleven Standard marketing territories. The Gulf Refining Company, the Indian Refining Company, the National Refining Company, the Pure Oil Company, and the Cudahy Refining Company all did business in at least two of the Standard marketing territories, and were able to make profits in competition with each other and with the Standard companies.

Moreover, the boundaries of the Standard territories were arbitrary. Almost without exception they conformed to state lines. And of course it is clear that state lines, being political boundaries, do not represent the most economical boundaries from the standpoint of distribution. Thus, the Standard Oil Company of Ohio, with a refinery in the northern part of the state, supplied the southern part of the state, in spite of the fact that the Standard Oil Company of New Jersey had a refinery at Parkersburg, West Virginia, just across the border. This division of territory, obviously uneconomical, would appear to have been adopted for the reason that such a division offered no opportunity for encroachment, thus avoiding disputes.

Further evidence of the absence of competition between the eleven Standard marketing companies was given by the marked unequalities in the price of gasoline in one territory as compared with another. The report gives numerous illustrations of these inequalities, but it suffices to say that they cannot be explained on the ground of differences in the cost of refining or of distribution. Had competition been effective these inequalities clearly could not have persisted. The Standard companies in low price territories would have made sales in the high price territories, and as a result there would have been eliminated all differences in price except such as were the result of differences in cost. It

is true that some Standard marketing concerns did make shipments into the territory of other Standard concerns; these interterritorial shipments amounted in 1915 to over 200,000,000 gallons. But these shipments represented sales to the company whose territory was "invaded," and the latter was therefore free to dispose of the gasoline as its own product, and at such prices as it saw fit. Obviously such sales had no tendency to equalize prices; they permitted each company to maintain the monopoly price that yielded it the maximum net profit. And this they were enabled to do by virtue of the dominant position which they occupied in the trade. The Commission estimated that the Standard companies controlled approximately 65 per cent of the gasoline business throughout the United States.[1] The "independents" thus controlled about 35 per cent; yet by no means all of their output could be regarded as competitive, since it included the sales of companies, such as the Tidewater Oil Company, in which the Standard stockholders had large interests. Moreover, the facts seemed to show that though the "independents" competed for business, they followed the *prices* fixed by the Standard companies in the several marketing areas.

The explanation of the lack of competition among the Standard marketing companies, according to the Federal Trade Commission, was to be found in the fact that there was a community of interest among these companies based on common stockholding. This community of interest, it should be noted, included the oil-producing, pipe-line, and refining companies, as well as the marketing companies. The stockholder lists of the Standard companies as of January, 1915, made it clear that although some changes in the personnel of the stockholders had taken place since the dissolution, a majority of the stock of most of the companies continued to be held by the same small group.[2] For example, 55 per cent of the stock of the Atlantic Refining

[1] Report of the Federal Trade Commission on Price of Gasoline in 1915, p. 143. The approximate percentage by territories is shown on p. 144.

[2] See Report of the Federal Trade Commission on Price of Gasoline in 1915, p. 145.

Company was held by the comparatively small group of individuals owning 300 shares or more apiece; and this same group held over 50 per cent of the stock of the Prairie Oil and Gas Company, the Prairie Pipe Line Company, the Continental Oil Company, and the Standard Oil companies of New Jersey, New York, Ohio, Indiana, Kentucky, and Nebraska. (If the holdings of less than 300 shares were included, the percentage of common holding would amount to approximately 70 per cent.) Moreover, the Standard Oil Company of New Jersey owned practically all of the stock of the Standard Oil Company of Louisiana and of the Carter Oil Company; and the presidents of the Standard Oil Company of New Jersey and the Standard Oil Company of New York owned about 70 per cent of the stock of the Magnolia Petroleum Company. A community of interest among the eleven Standard marketing companies and the crude oil and pipe-line companies was thus established.

In addition, the leading officers and directors of the Standard companies were frequently stockholders in several companies. To cite one instance, the president of the Standard of New Jersey owned 6,000 shares (worth $3,258,000 at the end of 1915) in his own company, 4,575 shares (worth $1,029,375) in the Standard of New York, 1,858 shares (worth $1,012,610) in the Standard of Indiana, 1,100 shares (worth $480,150) in the Prairie Oil and Gas Company, and 300 shares (worth $207,000) in the Atlantic Refining Company. Such common stockholdings naturally tended to restrain competition among the separate companies.

The conclusion of the Commission was that the combination, which was supposed to have been disintegrated, remained a combination in fact, if not in law,—a combination based on a community of interest, which in turn was the result of the interownership of stock.[1] In making this statement, however, the Commission was careful to say that it did not charge the Standard companies with violating the decree; for common ownership was not prohibited by the dissolution decree. Neither did it in-

[1] Report of the Federal Trade Commission on Price of Gasoline in 1915, p. 158.

tend to criticise the decree itself. The Standard Oil Company being the first important trust to be dissolved, the decree was more or less of an experiment. But it was the deliberate judgment of the Commission that the experiment of dissolving corporations without separating owners had not led to the desired result, which was the restoration of competition. In reply to the argument that some time in the future a redistribution of territory might be brought about by the "operation of economic laws," the Commission said that there was not sufficient evidence of a tendency to a substantial rearrangement of territory to warrant a reliance upon time and the laws of trade.

The Commission, therefore, in accordance with the duty imposed upon it by the Trade Commission Act, recommended that Congress enact legislation to remedy the unfortunate state of affairs thus disclosed. The suggestions, so far as they relate to common ownership, were: (1) A law providing for the reopening of anti-trust cases on the application of the Attorney General, for the purpose of securing such modifications of decrees as new conditions might require. (2) The abolition by legislation, in certain cases, of common stock ownership in corporations which have been members of a combination dissolved under the Sherman Act, when these companies are engaged in the same line of commerce. (3) As an alternative to (2), an effective limitation upon common ownership of stock in potentially competitive corporations by withdrawing the power of voting and control. (4) If Congress deemed it inadvisable to prevent common ownership, with its almost inevitable restriction of competition, the Commission recommended the enactment of legislation that would fix upon the common owners of stock in potentially competing concerns the responsibility for such acts of each of these concerns as resulted in the prevention of competition. With respect to the pipe-lines, the Commission urged that the best policy would be to apply the principle of the commodity clause, and segregate the ownership of the pipe-lines from the other branches of the petroleum industry. This would involve, said the Commission, a prohibition against the controlling portion of the stock of any pipe-line company engaged in interstate

commerce being owned by individuals or corporations that were also owners of crude oil or refining properties, or vice versa.

THE TOBACCO TRUST [1]

The dissolution of the tobacco trust—the next trust to be dissolved—presented a much more difficult problem than the dissolution of the oil trust. As the Supreme Court had pointed out, a mere decree forbidding stock ownership by one part of the combination in another part thereof would not afford adequate relief, since there would still remain corporations dominating various branches of the tobacco business. For example, to prescribe that the American Tobacco Company should part with its control of the American Snuff Company would not fully meet the situation, since the American Snuff Company would still dominate the snuff branch of the tobacco business in violation of the anti-trust act. Again, the subtle devices—to use the Court's language—that had been resorted to in establishing the trust were of such a character as to make it difficult, if not impossible, to formulate a remedy that would restore the prior lawful conditions. In view of this situation Justice Harlan recommended that the Supreme Court itself frame the dissolution decree, the record being sufficiently full, in his opinion, to enable the Court to formulate a plan. But the Court decided otherwise. It remanded the case to the court below, and directed it to hear the parties "for the purpose of ascertaining and determining upon some plan or method of dissolving the combination and of recreating, out of the elements now composing it, a new condition which shall be honestly in harmony with and not repugnant to the law." [2]

In view of the complex organization of the tobacco trust, the Circuit Court would have found its task sufficiently difficult,

[1] On the dissolution of the tobacco trust see especially: 191 Fed. Rep. 371–431; Report of the Senate Committee on Interstate Commerce on the Control of Corporations, 1913, pp. 315–350; Report of the Commissioner of Corporations on the Tobacco Industry, part III; Annual Reports of the Attorney General; and Muhse, Political Science Quarterly, 28, pp. 249–278.

[2] 221 U. S. 187.

even had the Supreme Court in other cases laid down the rules of dissolution. But except for the simple remedy provided in the Standard Oil case—a remedy which the Supreme Court had declared to be inadequate in the tobacco trust case—there were no rules. As the Circuit Court said, "We are left without guide to turn a condition in violation of the law into a condition honestly in harmony with it." [1]

The Circuit Court approached its problem by instituting a series of conferences between the counsel for the defendants and the counsel for the government (including the Attorney General), in order that a preliminary agreement upon the dissolution plan might be had. At these conferences, held in the presence of at least two members of the Court for a period of two months, many changes in the plan of dissolution suggested by counsel for the tobacco trust were made to meet the objections raised by the Attorney General. When affairs had finally reached such a stage that the differences between the parties could no longer be adjusted, the Court arranged for public hearings upon the matters yet in dispute; and at these hearings outside parties were given an opportunity to express their views. The plan proposed by the American Tobacco Company, modified in some respects as the result of these hearings, was then unanimously approved by the four circuit court judges, and made effective by a decree, entered November 16, 1911.

At these public hearings other plans for dissolving the trust were presented,—plans which in some instances differed widely from the plan of the defendants. But counsel for the defendants declared that they would not undertake to carry out any of these plans, preferring apparently to take their chances at receiver's sale. The Court therefore refused to consider them. It held that it had no power to enforce any plan of readjustment without the coöperation of the owners of the property.[2] Its only recourse, in the event that the proposed plan did not meet the requirements laid down by the Supreme Court, or in the event that the defendants would not accept such modifications as the Court might require, was, it said, to seize the property and sell

[1] 191 Fed. Rep. 386.

[2] Ibid., 375.

it at public auction. It would seem that if there was merit in these proposals of the outside parties the Court might properly have required their acceptance by the defendants as a condition of obtaining its approval of the plan; for the Court clearly was under no obligation to approve an unsatisfactory plan merely because the refusal of the defendants to accept it would necessitate a receiver's sale. Otherwise the Court might excuse itself for accepting any plan proposed by the defendants, no matter how inadequate it might be. But the Court apparently held a different view.

The decree in the tobacco case is the first instance in which a plan for the dissolution of a trust was elaborately worked out under the supervision of a court; and it therefore deserves detailed consideration. It is believed, however, that the details will be more readily understood, if the leading features of the plan are first summarized.

The plan of dissolution adopted by the Court provided for the division of the business of the trust among fourteen separate companies.[1] These companies, with the character of their business, were as follows: (1) American Tobacco Company (general tobacco manufacturing business, except snuff); (2) Liggett and Myers Tobacco Company (general tobacco manufacturing, except snuff); (3) P. Lorillard Company (general tobacco manufacturing, except snuff); (4) R. J. Reynolds Tobacco Company (general tobacco manufacturing, except snuff, cigarettes, and cigars); (5) Conley Foil Company (tin foil); (6) Johnston Tin Foil and Metal Company (tin foil); (7) MacAndrews and Forbes Company (licorice paste); (8) J. S. Young Company (licorice paste); (9) American Snuff Company (snuff); (10) George W. Helme Company (snuff); (11) Weyman-Bruton Company (snuff); (12) British-American Tobacco Company (general tobacco manufacturing in foreign countries); (13) Porto Rican-American Tobacco Company (cigars—Porto Rican and foreign); (14) United Cigar Stores Company (retail tobacco business).

The distribution of assets among these companies (or their

[1] The decree is in 191 Fed. Rep. 417–431.

stockholders), when the distribution took the form of stock, was effected by requiring the corporation owning such stock to distribute it to its own stockholders. For example, the American Tobacco Company was required to distribute among its shareholders the stock which it held in the American Snuff Company. The result was to vest in the stockholders of the American Tobacco Company the control formerly exercised by the American Tobacco Company as a corporation. The distribution of assets, when the assets were in the form of plants, was effected by requiring the dominant concern in any particular branch of the business to transfer a part of its factories to one or more other concerns, some of which were organized for the express purpose of meeting the requirements of the decree. For example, the American Tobacco Company was compelled to transfer some of its factories, brands, etc., to the Liggett and Myers Tobacco Company, a newly organized concern. The stock in the Liggett concern received by the American Tobacco Company as consideration for the transfer was then turned over by the American Tobacco Company to its own stockholders. None of the fourteen companies was allowed to hold stock in any of the other fourteen; and each of them, together with the individual defendants in the suit, was enjoined from continuing the illegal combination, or effecting a new one, by resort to a number of acts specifically dealt with in the decree of dissolution. The plan was to be carried into effect by February 28, 1912.

In a more detailed consideration, the dissolution decree may be described under the following headings: I. Abrogation of the domestic and foreign restrictive covenants; II. Disintegration of the accessory companies; III. Distribution by the American Tobacco Company of stocks owned or to be acquired by it; IV. Sale by the American Tobacco Company of manufacturing assets and business; V. Injunctions.

I. *Abrogation of the Domestic and Foreign Restrictive Covenants*

In acquiring the property or stock of competing concerns the tobacco trust had frequently stipulated as a condition of the purchase that the sellers sign an agreement not to reëngage in the

tobacco business. These covenants were to be rescinded; and the covenantors were thereafter to be permitted to engage in any branch of the business. The pooling agreement of September 27, 1902, under which the American Tobacco Company and the Imperial Tobacco Company had combined to form the British-American Tobacco Company was also to be cancelled.

II. *Disintegration of the Accessory Companies*

The five companies designated by the Supreme Court as accessory companies (because accessory to the combination) were: (1) American Snuff Company; (2) MacAndrews and Forbes Company; (3) Conley Foil Company; (4) American Stogie Company; and (5) American Cigar Company. The decree dealt specifically with each of these companies.

The American Snuff Company had a monopoly of the manufacture of snuff; in 1910 it produced 96.5 per cent of the total output. By the decree there were to be organized two new snuff companies (the George W. Helme Company and the Weyman-Bruton Company), and to these new companies the American Snuff Company was to turn over a number of its factories with the brands manufactured therein. From each of these corporations the American Snuff Company was to receive $4,000,000 common stock and $4,000,000 voting preferred stock,—a total of $16,000,000. The common stock of these two companies the American Snuff Company was to distribute, as a dividend, to its own common stockholders; and the preferred stock it was to offer at par to its preferred stockholders in exchange for their preferred stock in the American Snuff Company. As by this process of exchange the American Company came into possession of its own preferred stock, it was to retire it; but it was not to use the preferred stock in the two new companies that it continued to hold, because of the failure of its preferred stockholders to make the exchange, as a means of exercising control over their operations. In any event, the American Snuff Company by exchange or sale was to dispose of the preferred stock of the two new companies by January 1, 1915. The American Tobacco Company as a stockholder in the American Snuff Com-

pany would of course receive stock in the Helme Company and the Weyman-Bruton Company; but this stock, as well as its stock in the American Snuff Company, was in turn, as will be pointed out shortly, to be distributed by the American Tobacco Company to its stockholders.

The disintegration of the other four accessory companies followed substantially this plan, though provision was made for the dissolution of the American Stogie Company. Moreover, in the case of the American Cigar Company, the American Tobacco Company continued to hold control, instead of being compelled to distribute the stock of this company to its own shareholders, as was the usual arrangement.

III. *Distribution by the American Tobacco Company of Stocks Owned or to be Acquired by it*

The dissolution decree as thus far described would leave the American Tobacco Company in possession of the securities of a number of companies, including certain ones not dissolved by the decree.[1] But these stocks, with only a few exceptions, were to be disposed of by the American Tobacco Company, some immediately, and the remainder by January 1, 1915. Meanwhile the American Tobacco Company was not to attempt to exercise any influence or control over these companies.

IV. *Sale by the American Tobacco Company of Manufacturing Assets and Business*

The American Tobacco Company, even after it had disposed of its interest in the snuff, licorice, and tin foil companies would still be an illegal combination by virtue of its domination of

[1] Particularly the R. J. Reynolds Tobacco Company, the British-American Tobacco Company, the Porto Rican-American Tobacco Company, and the United Cigar Stores Company. These companies, all subsidiaries of the American Tobacco Company, were not held by the Supreme Court to be illegal in themselves; and their property was therefore left intact. But their domination by the American Tobacco Company was held illegal, and they were therefore detached from that company by a requirement that the American Tobacco Company distribute to its own stockholders its holdings of stocks in these companies.

the cigarette, plug, smoking tobacco, fine-cut, and little cigar branches. It was therefore necessary to transfer a part of these businesses to other concerns. The decree consequently provided that the American Tobacco Company should give to its common stockholders the stock that it held in the R. J. Reynolds Tobacco Company,—a concern manufacturing mainly plug tobacco, but also some smoking tobacco. It was next provided that two new companies be organized—the Liggett and Myers Tobacco Company and the P. Lorillard Company [1]—and to these companies the American Tobacco Company was to convey numerous factories and brands, including raw materials, storage houses, and cash, in order that both of the new concerns might be "fully equipped" for the conduct of the tobacco business.

The properties, brands, and good will to be conveyed to the Liggett and Myers Tobacco Company were valued at $67,447,499; and those to be conveyed to P. Lorillard Company were valued at $47,552,501. (The American Tobacco Company would be left with assets valued at $98,432,473.83, upon which its earnings, based on the results for 1910, would be $11,369,809 or 11.55 per cent.) Both of these new companies were to pay for the properties received by them in their own securities, these securities to consist of 7 per cent bonds, 5 per cent bonds, 7 per cent preferred stock, and common stock. These securities, aggregating $115,000,000, and constituting practically the total capitalization of the new companies, were then to be disposed of by the American Tobacco Company, some by March 1, 1912, the balance within three years.

V. *Injunctions*

The defendants, their officers, directors, servants, agents, and employees were enjoined from continuing the illegal combination, and from entering any similar one, the effect of which would be to restrain interstate or foreign commerce in tobacco or its products, by resort to any of the following acts: (1) By con-

[1] A company of the same name then in existence was to be wound up, and its assets delivered to the new company. The old Liggett and Myers concern had been dissolved in the merger of 1904.

veying the factories, brands, or business of any of the fourteen corporations among which the properties of the combination were divided to any other of these corporations, either by placing the stocks of any one or more of them in the hands of voting trustees, or by controlling the voting power of these stocks by any similar device. (2) By making any express or implied agreement relative to the control of any of the fourteen corporations, or relative to the purchase, sale, transportation, or manufacture of tobacco or its products or supplies, which would have a like effect in restraint of commerce to that of the combination, the operation of which had been enjoined; or by making any arrangement of any kind with any other of these corporations for the apportionment of trade among them, in respect either to customers or localities. (3) By any two of the fourteen corporations employing the same clerical organization or keeping the same offices. (4) By any of the fourteen corporations holding stock in any other corporation any part of the stock of which was also held by any other of these corporations.[1] (5) By any of the fourteen corporations doing business, directly or indirectly, under any other than its corporate name or the name of a subsidiary corporation controlled by it; provided, that in the case of a subsidiary company the controlling corporation should cause the products of the subsidiary to bear a statement indicating the fact of such control. (6) By any of the fourteen corporations refusing to sell to a jobber any brand of tobacco manufactured by it, except upon the condition that the jobber should purchase from the seller some other brand or product also manufactured by it; provided, however, that this prohibition should not be construed to apply to what were known as "combination orders," under which a brand or product might be offered to a jobber at a reduced price, on condition that he purchase a given quantity of some other brand or product.[2]

[1] Certain minor exceptions were allowed.

[2] This proviso was inserted by the Court in order that the fourteen corporations might not be estopped from employing methods of business which were open to and practiced by all their competitors. 191 Fed. Rep. 381.

It was further decreed that for a period of five years from the date of the decree the fourteen corporations, their officers, directors, etc., were enjoined: (a) from having any officers or directors in common ; (b) from having any common agents for the purchase in the United States of tobacco leaf or other raw material, or for the sale in the United States of tobacco or other products; and (c) from acquiring, directly or indirectly, stock in any other of the fourteen corporations, or from acquiring their factories, brands, or business, or from extending them financial aid.

Finally, each of the twenty-nine individual defendants was enjoined during a period of three years after the date of the decree from holding, directly or indirectly, stock, or a legal or equitable interest in stock, in any one of the fourteen corporations (except the British-American Tobacco Company), in excess of the amount to which he was entitled under the dissolution plan; provided, however, that any of the defendants might, notwithstanding this prohibition, acquire from *other defendants*, or from their estates in the event of their death, stock held by such defendants in any of the fourteen corporations.

Jurisdiction of the case was retained by the Circuit Court in order that it might be in a position to issue further decrees, should such become necessary to carry out the mandate of the Supreme Court. But the jurisdiction thus retained was of a limited sort. The Attorney General had requested that the Court reserve to the government the right at any time within five years to make application for further relief, if it appeared that the plan of dissolution had not created a new condition in harmony with the law. But the Court held that it had no such power. Had it not been for the mandate of the Supreme Court it would even have questioned its jurisdiction to recreate a new group of corporations out of the elements into which the combination had been split. The mandate of the Supreme Court had settled that question, it said, but this gave no warrant for the conclusion that the lower court might prescribe the temporary terms of a modus vivendi, with power subsequently to modify

these terms.[1] The request of the government was therefore denied.

The plan of dissolution as just outlined was thus comprehensive. By many it was hailed as a great triumph for the government; by others it was derided as a farce. The former view was expressed by William Howard Taft, formerly a judge in the federal courts, and learned in the law. While President of the United States he said: "I venture to say that not in the history of American law has a decree more effective for such a purpose been entered by a court than that against the Tobacco Trust." [2] On the other hand, Mr. Louis D. Brandeis, prior to his appointment to the Supreme Court, said that the net effect of the dissolution was to legalize a combination heretofore illegal.[3] He testified before a Senate Committee in December, 1911, that the decree of the court was regarded as a "certificate of good character," and that the plight of the independent tobacco manufacturers was worse, in his opinion, than it had been before.[4] Mr. Samuel Untermyer, a well-known New York lawyer, in testimony before the same committee referred to the "pitiful and humiliating fiasco in the tobacco case." [5] In his opinion the decree was "the most colossal judicial farce ever enacted." [6]

In the light of such strong language it is fitting to examine the objections to the decree, particularly those raised by counsel for the independent tobacco manufacturers. Their opinion is especially significant in view of the fact that among their number was Mr. Louis D. Brandeis, who was later appointed to the Supreme Court (1916), and who might be expected to play an important part in the ultimate solution of the larger problem raised by this case.

The Court having given outside parties leave to be heard on the plan of dissolution proposed by the American Tobacco

[1] 191 Fed. Rep. 384.
[2] Congressional Record, December 5, 1911, p. 23.
[3] World To-Day, 21, p. 1441 (December, 1911).
[4] Report of the Senate Committee on Control of Corporations, p. 1255.
[5] Ibid., p. 181.
[6] Ibid., p. 206.

Company, Messrs. Louis D. Brandeis and Felix H. Levy, as counsel for the National Cigar Leaf Tobacco Association, the Cigar Manufacturers' Association, and the Independent Tobacco Salesmen's Association, filed a statement on October 25, 1911, three weeks before the decree of the Court was entered, criticising the plan of dissolution.[1] In view of the fact that the Court rejected most of the suggestions made in this brief, this criticism of the proposed dissolution would likewise apply for the most part to the court decree of November 16. In those instances in which this is not true, that is, where the Court admitted the force of the criticism and revised the decree accordingly, the fact will be stated.

According to the brief filed by Messrs Brandeis and Levy, the plan, if approved, would result in legalizing monopoly, instead of restoring competition.[2] The plan, they held, contained five fundamental defects, each so serious as to furnish in itself sufficient ground for the rejection of the plan. These defects were classified under the following headings: I. Common ownership; II. Dominating concerns; III. Completely equipped concerns; IV. Restraints on unfair competition; V. United Cigar Stores Company.

I. *Common Ownership*

The main objection to the plan was the common ownership of the leading concerns into which the trust was split. This common ownership resulted, of course, from the distribution by the American Tobacco Company to its own stockholders of the securities which it had formerly held. By this distribution the control which had been exercised by the American Tobacco Company in its corporate capacity was transferred to its own stockholders. It is true that the control was by no means as concentrated as before. Prior to the dissolution the twenty-nine individual defendants had owned about 56 per cent of the common stock of the American Tobacco Company,

[1] Given in full in Report of the Senate Committee on Control of Corporations, pp. 315–322.

[2] Report of the Senate Committee on Control of Corporations, p. 315.

which, in view of the fact that the preferred stock carried no voting power, gave them control of the Combination.[1] But by the dissolution decree the preferred stock was given voting privileges. And since the preferred stock exceeded the common stock in amount, and since the individual defendants held a decidedly lower percentage of the preferred stock than of the common, the result was that they received an average of only 35 per cent of the voting stock in the fourteen corporations. But, as counsel for the independents pointed out, the individual defendants held a sufficiently large minority interest to control all the separate companies, providing the majority stockholders did not unite against them. And in view of the past affiliations of these stockholders such united action on the part of the majority was improbable. Counsel therefore insisted that the proposed plan would not be effective to restore competition, since it did not provide that the separate corporations which were to continue the business of the trust should at the outset and for a limited period thereafter be owned by absolutely distinct groups of individuals.

With respect to the first argument, the Court conceded that the defendants, though holding only a minority interest, might control the fourteen companies. But it held that it had done its duty if it saw to it that the *legal* control of the corporations was taken out of the hands of the defendants.[2] The Court did not feel that it was called upon to guard against the possible failure of the majority to exercise its power. With respect to the argument that whenever there existed common stockholding there would be no real competition, the Court held that since the Supreme Court in both the Northern Securities and Standard Oil cases had not indicated disapproval of a method of disintegration that left the separate concerns into which these combinations were divided in the hands of the same body of stockholders, the question as to whether common stockholding was repugnant to the law had been settled for it by controlling

[1] Report of the Commissioner of Corporations on the Tobacco Industry, part III, p. 213.

[2] 191 Fed. Rep. 388. Italics supplied by the author.

authority.[1] It is true, said the Court, that the highest tribunal in deciding these cases did not discuss the question of "common ownership," but its existence in both cases was so plainly manifest that it was difficult to understand how the Court could have approved of the new arrangement, unless it was satisfied that it did not contain the same vice as the one which had been declared illegal. The government also seemed to hold this view, said the Court, for it did not discuss common stockholding.

II. *Dominating Concerns*

The next objection to the plan was that it created a few dominating concerns. The four corporations that were to conduct the cigarette, plug, smoking, fine-cut, and little cigar business of the trust were given such a large percentage of the country's trade in each of these lines as to enable them, it was claimed, to dominate the independents, whether planters, manufacturers, or dealers, and thus unreasonably to restrain trade.

The distribution of the tobacco business among the various concerns as of 1910 is given in a table reproduced in the decision of the court.[2] This table shows that the cigarette business of the trust was divided among three concerns, which would produce, on the basis of the figures for 1910, 33.15 per cent, 21.03 per cent, and 26.02 per cent, respectively, in value, of the entire cigarette business of the country. And the distribution of brands of cigarettes among the three "colorable" competitors was such, counsel alleged, that each of them would, as against the other two, dominate a particular branch of the tobacco trade. The combined independent production, on the other hand, was only 19.80 per cent, or less than that of either of the three dominating companies. Mr. Brandeis held that the cigarette business of the trust, representing the absorption of eighteen separate concerns, should have been divided among at least seven separate companies, instead of among only three.

The smoking tobacco business of the trust was divided among

[1] 191 Fed. Rep. 375–376. But see U. S. *v.* Union Pacific Railroad Company, 226 U. S. 470, where the Supreme Court took a different view.

[2] 191 Fed. Rep. 411.

four companies, producing 40.53 per cent, 16.47 per cent, 18.88 per cent and 2.73 per cent, respectively, of the total value of the smoking tobacco output. The combined independent output was only 21.39 per cent, or about half that of the American Tobacco Company, and only slightly larger than that of the two other leading producers. Counsel for the independents maintained that the smoking tobacco business of the trust, the result of combining fifty-seven separate businesses, should have been divided among at least twelve concerns.

It is not necessary to carry this analysis through every branch of the industry; yet attention should be called to the position of the independents in the little cigar business. The Liggett and Myers Tobacco Company was given 43.78 per cent of the output (not value) of little cigars, whereas the combined independent production amounted to only 6.95 per cent. It was thus to be expected that the Liggett and Myers Company would do a business six times greater than that of the independents. Yet this could hardly have been avoided. The Liggett and Myers output of little cigars consisted of only a single brand, and it is difficult to see how this could have been divided.[1] This illustration goes to show how the Combination's policy of concentrating on a few leading brands rendered more difficult the framing of an effective plan of dissolution. Any company which received one of these principal brands would of necessity have a large proportion of the total trade in that branch. In the cigar business, as distinguished from the little cigar business, the situation was different. The Combination, for reasons pointed out elsewhere,[2] had never been able to dominate the cigar branch. The independents thus continued to retain the ascendancy, producing 86.64 per cent of the total output.

Objection was also made to the dominant position given to the licorice and tin foil companies. The MacAndrews and Forbes Company, a majority of the stock of which had been owned by the American Tobacco Company, produced prior to

[1] Report of the Commissioner of Corporations on the Tobacco Industry, part III, p. 215.

[2] See p. 132.

the dissolution about 90 per cent of the licorice paste manufactured in the United States.[1] By the decree it was forced to turn over its Baltimore plant to a new company, but this still left it, according to Mr. Brandeis, 60 per cent of the licorice paste business of the country. Does this mean that, in the opinion of the Circuit Court, the control of 60 per cent of the supply of a commodity is legal under the Sherman Act?

III. *Completely Equipped Concerns*

The decree provided that the two new companies which received a part of the manufacturing properties of the American Tobacco Company—Liggett and Myers, and P. Lorillard—should be "fully equipped for the conduct of the business of manufacturing and dealing in tobacco."[2] Mr. Brandeis claimed that no independent concern was "completely equipped for the conduct of a large tobacco business"; and that no plan to restore competition would prove effective which did not ensure that the several concerns that were to continue the business formerly done by the trust were, at the outset, of a character similar to the independent concerns. The American Tobacco Company, for example, was given a cigarette department with 33.15 per cent, in value, of the whole cigarette business of the country, a smoking department with 40.53 per cent of the country's total, a plug department with 22.98 per cent, etc. Its business extended over nearly every branch of the tobacco trade; in each branch it had a large percentage as compared with any independent concern; and it was to receive, with Liggett and Myers, and P. Lorillard, brands of tobacco practically indispensable to the successful conduct of the jobbing or retail business. By means of these "indispensable brands" it would be able, it was alleged, to compel dealers to give preference to its other products as against the products of independents; and the large profits on these indispensable brands could be used to crush the independents in the branches in which they competed. It was therefore urged that no concern taking over any part of the cigarette business of

[1] 191 Fed. Rep. 394.

[2] Ibid., 424.

the trust should be given any of the smoking tobacco, plug, or cigar business.

On this matter the Court said: "Manifestly the minuter the fragments into which the old combination is split, and the more they are prohibited from conducting business as other companies are free to conduct it, the less will be their ability to compete with such other companies. This whole line of argument deals with the *economics* [1] of the tobacco business. No doubt the novel problem presented to this court is connected with questions of economics as well as with questions of law. But this is a court of law, not a commerce commission, and the legal side of the proposition would seem to be the controlling one." [2] Judge Lacombe then went on to say that the true way to approach the problem would be to consider whether a group of companies, organized as these fourteen corporations were, and enjoined as they were by the decree, would be held by the Supreme Court to be repugnant to the law. And his conclusion from a study of the Standard Oil and Tobacco decisions was that the Court would not find them to be in violation of the Sherman Act.

IV. *Restraints on Unfair Competition*

The brief filed by Messrs Brandeis and Levy objected to the plan because it contained no injunction against those methods of unfair competition by means of which the trust in the past had destroyed its competitors. This defect, however, was remedied; the Court, as was pointed out in the section on Injunctions, enjoined the defendants against a continuance of the illegal combination, and enumerated certain acts that were specifically prohibited. Certain requests of the independents, however, were denied by the Court. These requests (in part) and the Court's replies were: [3] (1) That each of the fourteen corporations be restrained "from espionage on the business of any competitor either through bribery of any agent or employee of such competitor, or obtaining information from any United

[1] Italics supplied by the author.

[2] 191 Fed. Rep. 376.

[3] Report of the Senate Committee on Control of Corporations, p. 320.

States revenue official." The Court said that it failed to see why a corporation could not legitimately obtain from private or public sources information as to the business of a competitor, and when illegitimate methods were proved, they might be dealt with.[1] (2) That the fourteen corporations be restrained "from giving away, selling at or below the cost of manufacture and distribution, any of its products, or adopting any other method of cutthroat competition for the purpose of destroying or of acquiring the business or trade of a competitor," and (3) "from refusing to sell to any jobber any brand of snuff or cigarettes or smoking or chewing tobacco manufactured by it which is indispensable in the particular market. It should also be restrained from giving any rebates, allowances, or other special inducements to those who use its goods exclusively or give preference to them over the goods of competitors." The Court refused both of these requests. It pointed out that these were common methods in the tobacco trade, practiced by all alike. Only by the giving away of samples, or by the offering of very favorable terms, could new brands be introduced, or old brands be extended into new territory. These methods being employed by the other companies, and being obnoxious to no statute, there was no reason, so the Court said, why the fourteen corporations should be enjoined against their use.[2] (4) That "every independent or other person interested should in the event of any alleged violation of the injunction have liberty to apply to the court for protection and such action as may appear to be appropriate." The Court denied this request from a fear that it would be overwhelmed with a multitude of applications, mainly frivolous. It held that any one who felt that he had a grievance should take the complaint to the Attorney General, who, if he found substance in it, could bring it before the Court.[3]

V. *United Cigar Stores Company*

The dissolution plan provided that the United Cigar Stores Company should be left intact, but that the American Tobacco

[1] 191 Fed. Rep. 381. [2] Ibid. [3] Ibid., 382.

Company should distribute its stock in this company among its own stockholders. Mr. Brandeis declared that the power of the United Cigar Stores Company was so great that its continued existence would render effective competition improbable, even if the manufacturing properties of the trust were divided among companies having different stockholders. He held that the property and business of this company ought to be distributed among at least ten separate corporations, each with a different set of stockholders, and none with a predominant power in any locality. The Court, however, refused to grant this relief. It pointed out that the Attorney General had not requested it. All that the Attorney General urged was that the stock of the United Cigar Stores Company be distributed by means of a sale to others than the twenty-nine individual defendants or the remaining stockholders of the American Tobacco Company, in order that the company might be separated entirely from the rest of the fourteen corporations. But the Court, so it held, was without power to grant even this request.[1] The United Cigar Stores Company therefore was left undisturbed.

This review of the defects of the plan of dissolution shows that there is grave doubt whether a new condition honestly in harmony with the anti-trust law was in fact created. It was therefore eminently desirable that the matter should go to the Supreme Court for its approval or disapproval. But unfortunately there was no way whereby it could reach the Supreme Court, so long as the lower court and the two parties to the suit were satisfied. Counsel for the independents had endeavored to secure the insertion in the decree of a clause directing the submission of the plan to the Supreme Court for review, but the Attorney General had objected, and the request was denied.[2] Upon the rendering of the decree the independents appealed to the Supreme Court for a review of the order of the lower court, but this was refused on December 11, 1911.[3] The Sherman Act contains no provision whereby parties other than the Attorney

[1] 191 Fed. Rep. 383.

[2] Report of the Senate Committee on Control of Corporations, p. 357.

[3] Chron., 93, p. 1670 (December 16, 1911).

General who brought the suit can intervene, and necessarily therefore the petition of the independents was denied by the Supreme Court. Subsequently (April, 1912) the Senate passed a bill directing the Attorney General to appeal, but this measure was not acted upon in the House. Clearly this outcome of the whole affair is unfortunate. The lower courts have been reversed so frequently by the Supreme Court on difficult questions of law that a final settlement of this matter by our highest court should have been had, particularly in view of the many other trust cases on the Court's docket. The failure of Congress to pass the bill might, moreover, be reasonably regarded as having given the fourteen corporations vested rights, since they were reorganized in accordance with a court decree.

No complete investigation of the effects of the dissolution decree has yet been made. The Bureau of Corporations published in 1915 a report on prices, costs, and profits in the tobacco industry, in which it compared the prices, costs, and profits of the Combination from 1893 to 1910 with those of the successor companies from 1912 to 1913.[1] But the Bureau did not go into the other matters that bore on the effectiveness of the dissolution, for the reason that the Department of Justice was then making an investigation of the manner in which the decree was being observed. Moreover, the report did not cover the accessory companies (those manufacturing tin foil, licorice, etc.), the domestic retail business, nor the foreign business. It was limited to the successor companies, which included the American Tobacco Company, the Liggett and Myers Tobacco Company, the P. Lorillard Company, the R. J. Reynolds Tobacco Company, the American Snuff Company, the George W. Helme Company, and the Weyman-Bruton Company.

The report of the Bureau, though incomplete, gave certain data significant in this connection.[2] (1) The report showed that the successor companies did a slightly larger percentage

[1] Report of the Commissioner of Corporations on the Tobacco Industry, part III.

[2] For the conclusions of the Bureau as to the effect of the dissolution on manufacturing and selling costs, see pp. 147 seq.

of the tobacco business of the country than did the trust which preceded it. This is indicated by the table below.[1]

Branch	*Proportion manufactured by the trust in 1910*	*Proportion manufactured by the successor companies in 1913*
Plug	84.5	84.7
Little cigars	91.4	91.0
Smoking	76.1	73.4
Fine-cut	79.7	77.2
Cigarettes	83.9	90.7
Snuff	96.5	97.3

From this table it appears that the percentage of the successor companies in the plug branch increased slightly, while their percentage of the little cigar branch declined slightly, as compared with the business of the trust in 1910. In the smoking and fine-cut branches there was a more noticeable decrease in the proportion of the country's output controlled by the successor companies. But the control over the cigarette branch was much increased. Whereas the trust had controlled only 83.9 per cent of the cigarette business in 1910, the successor companies in 1913 controlled 90.7 per cent. Both the American Tobacco Company and the Liggett and Myers concern sold in 1913 about seven times as many cigarettes as the five largest manufacturers in the country other than the successor companies.[2] And in snuff the high degree of monopolistic control possessed by the trust was further increased. The three successor companies in 1913 produced 97.3 per cent of the total output, a close approach to the complete elimination of the independent element. And even if these three companies had been required to have separate stockholders, as was urged by the independents, competition among them would have been unlikely. This was because the division of brands under the dissolution decree gave each of them a practical monopoly in a distinct sales terri-

[1] Report of the Commissioner of Corporations on the Tobacco Industry, part III, p. 11.

[2] Ibid.

tory, thus effecting a practical division of the field.[1] As a result, the Bureau reported, competition among them was inactive; and profits were higher, and selling costs lower, than in any other branch of the tobacco industry.

(2) The report showed that in most branches of the tobacco business the output of the successor companies was divided among them more evenly in 1913 than it had been directly after the dissolution.[2] In other words, the successor companies with a high percentage of a particular branch had lost ground relatively to the successor companies with a lower percentage of that branch. A marked exception was the Liggett and Myers concern in its plug business. This company was given (by the dissolution decree) 33.83 per cent of the total output of plug tobacco; but by 1913 its percentage had increased to over 40 per cent of the total.[3]

(3) The report showed that such competition as there was among the successor companies largely took the form of greatly increased advertising expenditures, extension of sales territories, and an attempt to fill in the gaps in their business in which they were weak.[4]

(4) Finally, the report brought out that there had been no decided changes in prices to the jobbers or to the consumers since the dissolution of the trust.[5] These facts, taken in conjunction with the large profits realized, show that such competition as took place did not manifest itself in prices. This absence of competition in prices was to be explained in part by the price making conditions of the tobacco trade, and in part by statutory provisions. Tobacco products at that time were nearly always sold at retail at five cents per package, or some multiple of five cents. Had the jobber reduced the price to the retailer, the effect in most cases would have been merely to

[1] Report on the Tobacco Industry, part III, p. 14.

[2] Ibid., p. 11.

[3] Calculated from data in the Report on the Tobacco Industry, part III, pp. 221–222.

[4] Report on the Tobacco Industry, part III, pp. 13–14.

[5] Ibid., p. 23.

increase the retailers' profit without affecting the price at which he would have sold to the consumer. And though a reduction in the price to the jobber on any particular brand might have caused the jobber to push the article more energetically, it was generally more profitable for the manufacturer to maintain the price to the jobber, and to force him to buy by means of elaborate advertising, which created a demand on the part of the consumer, and thus compelled the retailer and the jobber to buy the advertised article. Notwithstanding the foregoing considerations a reduction in prices might have taken place through the selling of a larger package for the same price. This, however, did not occur, except in rare instances, being prevented by the statutory provisions fixing the size of packages. To illustrate, the law provided that smoking tobacco might be put up in packages of one-half an ounce, three-quarters of an ounce, one ounce, etc., up to four ounces. The leading size as a matter of fact was the two ounce package, which for high grade smoking tobacco generally retailed at 10 cents, or 80 cents per pound. Had a manufacturer competing for business desired to increase the size of his package he would have been forced to increase it to two and one-quarter ounces. This, if sold at 10 cents per package, would be at the rate of 71.1 cents per pound. The manufacturer, if he desired to charge the jobber the same price, would thus receive 8.9 cents less per pound; and this he could not afford to do, since no important brand of smoking tobacco sold by any of the successor companies in 1913 yielded a net profit of this amount.[1] Obviously, therefore, no increase in the size of the package was possible as matters then stood. This condition, it may be observed, held good for all tobacco products except those put up in the larger packages, that is, those over four ounces (these formed but a small percentage of the total sales), and except for plug tobacco, which the manufacturer and the retailer were practically free to sell in any size that they chose. Therefore, without further legislation permitting smaller differences in the size of the package than one-quarter of an ounce, or permitting all tobacco products to be packed and

[1] Report on the Tobacco Industry, part III, p. 24.

stamped in wholesale quantities, no real competition in prices was to be expected.

THE POWDER TRUST

The proceedings against the powder trust were brought on July 30, 1907, and a unanimous decision in favor of the government was rendered by the Circuit Court on June 21, 1911.[1] The trust did not appeal from this decision; but proceeded at once to negotiate with the Department of Justice concerning the details of the plan of dissolution. An agreement having been reached, a final decree was entered on June 13, 1912.[2] The decree of the court bore a striking resemblance to the decree in the tobacco trust case, and therefore a brief description will suffice.[3]

The final decree dismissed the petition as to sixteen of the defendants, and dissolved the monopoly maintained by the remaining twenty-seven defendants (twelve corporate and fifteen individual). Eight of the corporate defendants were ordered to dissolve, and to distribute their property among their own stockholders; and three were left undisturbed, so far as their corporate organization was concerned. The remaining corporate defendant was the E. I. du Pont de Nemours Powder Company, the owner of most of the property embraced in the trust. This company was permitted to retain twenty-one of its powder plants, but was obliged to transfer to two new corporations—the Hercules Powder Company and the Atlas Powder Company, both organized for this purpose—its remaining plants, twenty-two in number. In general, the distribution of plants under the decree was such as to make the restoration of competition feasible.

The defendants were enjoined from continuing the illegal combination, and from forming by any device whatsoever any like combination. The dissolution plan was to be put into

[1] 188 Fed. Rep. 127–156 (June 21, 1911).

[2] A copy of the decree is in Decrees and Judgments in Federal Anti-Trust Cases, pp. 195 seq.

[3] On the dissolution of the powder trust, see Stevens, Quarterly Journal of Economics, 27, pp. 202–207.

operation by December 15, 1912; and the court retained jurisdiction of the case for the purpose of making such further orders as might prove necessary.

While no investigation has been made as yet into the results of the dissolution, it is certain that to date they have been slight. Within two years after the decree of the Court the war broke out, and down to the close of 1918 the demand for powder was so great that the facilities of powder manufacturers were taxed to the utmost. Prices naturally advanced; and probably the amount of the advance was entirely unaffected by the presence or absence of competitive conditions in the industry. For whenever the demand far outstrips the supply, a competitive price is likely to be the same as a monopoly price, unless the monopoly curtails the supply, as would be quite improbable under the conditions prevailing during 1914–1918. With the termination of hostilities in November, 1918, the demand for powder declined, and prices naturally fell. But meanwhile as the result of the war the general price level for commodities had fundamentally, and perhaps permanently, changed. Even a governmental body with large powers would thus have difficulty in determining the effect of the dissolution on the price of powder. The matter is complicated, moreover, by the fact that the tremendous prosperity of powder companies during the war attracted into the field a host of new concerns, whose competition, if effective, might conceivably bring the price of powder temporarily below a remunerative level. In the light of these facts, it appears that to trace with any approach to accuracy the effect of the dissolution on prices is difficult, if not impossible.

THE SHOE MACHINERY TRUST

Since the fall of 1911 at least four separate proceedings have been instituted by the government against the United Shoe Machinery Company or its officers. The first was a criminal suit brought on September 19, 1911, against the president and other officers of the company, charging them with engaging in a combination and conspiracy in restraint of trade. The de-

cision of the Supreme Court dismissing this case has already been described.[1]

The second was a civil suit instituted on December 12, 1911, asking for the dissolution of the shoe machinery trust. The District Court on March 18, 1915, and the Supreme Court on May 20, 1918, decided adversely to the government. The Supreme Court, as elsewhere noted,[2] held that the companies that were combined in the United Shoe Machinery Company in 1899 were complementary, and not competitive. These companies prior to 1899 had individually monopolized various branches of the shoe machinery business, but they were patent monopolies protected by law, and hence their union in a single company was not illegal. The government had also attacked the leases of the United Company, and in particular the so-called tying clauses. But the Supreme Court held that the leases were simply the exercise of the company's right as a patentee.

The third was a proceeding to enjoin a contract alleged to be in restraint of trade in "inseam trimming machines."[3] The petition of the government was filed on February 8, 1913. The prosecution of the case was not pushed, the government preferring to await a decision in the dissolution suit; and presumably with the loss of that case the ancillary proceeding was dropped.

The fourth was an attack on the tying clauses in the shoe machinery leases. These leases had been upheld by the Supreme Court in its decision of May 20, 1918; but subsequent to the bringing of this earlier suit the Clayton Act was passed, and the government brought a new proceeding, on October 18, 1915, charging that the leases violated section three of the Clayton Act. The District Court rendered a decision favorable to the government on March 31, 1920;[4] but the case was appealed to the Supreme Court.

[1] See p. 431 (U. S. *v.* Winslow).

[2] See p. 432 (U. S. *v.* United Shoe Machinery Company).

[3] Annual Report of the Attorney General, 1913, p. 14.

[4] 264 Fed. Rep. 138.

THE CASH REGISTER TRUST

A civil suit against the National Cash Register Company was instituted on December 4, 1911.[1] The government alleged a conspiracy to restrain and monopolize trade in cash registers; and asked the Court to enjoin the continuance of the conspiracy and attempted monopoly, and also to enjoin a number of unfair competitive methods.[2] On February 22, 1912, a criminal proceeding was begun against the president of the company and twenty-nine other officials, the charges being substantially the same as in the civil suit.[3] As the prosecution of the civil case was delayed, pending the settlement of the criminal case, the outcome of the latter may be briefly noted. A demurrer to the indictment having been overruled by the district court on June 26, 1912,[4] the defendants, with only one exception, were found guilty, and jail sentences ranging from nine months to one year and fines aggregating $135,000 were imposed.[5] An appeal was taken to the Circuit Court of Appeals, where the conviction was set aside on March 13, 1915.[6] The government applied to the Supreme Court for a writ of certiorari, which was denied on June 14, 1915.[7] Thereupon the government concluded not to press the case further.

Despite the loss of the criminal suit the government decided to push the civil suit to a conclusion. A decision in the case was never rendered, however; for on February 1, 1916, the National Cash Register Company consented to the entry of a decree.

The decree granted substantially the relief asked by the government in its petition.[8] It did not, to be sure, enjoin the

[1] The Federal Antitrust Laws, July 1, 1916, p. 70. For an account of an earlier suit see p. 441.

[2] Petition in United States v. National Cash Register Company, pp. 31–38.

[3] The Federal Antitrust Laws, July 1, 1916, pp. 73–74.

[4] 201 Fed. Rep. 697.

[5] Decrees and Judgments in Federal Anti-Trust Cases, pp. 795–798.

[6] 222 Fed. Rep. 599.

[7] 238 U. S. 635.

[8] A copy of the decree is in Decrees and Judgments in Federal Anti-Trust Cases, pp. 315–320.

company against further attempting to monopolize interstate commerce in cash registers, nor did it prohibit in sweeping fashion, as requested by the government, the suppression of competition. But it did find that the company had combined to restrain and monopolize trade, and it enjoined the company and its directors, officers, agents, and employees from committing a number of acts. A summary of the acts enjoined well shows the character of the methods whereby the company, aided in considerable measure by the possession of valuable patents, had been able to secure control of 95 per cent of the business of manufacturing cash registers.[1]

The acts specifically prohibited by the Court were: (1) inducing purchasers of competing cash registers to repudiate the contract of purchase; (2) espionage upon the business of competitors; (3) inducing employees or agents of competitors and dealers in competing machines to sever their connection with the competing concerns; (4) manufacturing or selling cash registers made to resemble competing registers, when sold for the dominant purpose of preventing sales of competing registers; or selling cash registers at a price fixed with reference, not to the cost of manufacture, but to the price of competing machines, for the purpose of eliminating competitors from business; (5) selling competing cash registers, whether obtained by purchase, exchange, or otherwise, for the purpose of preventing sales by competitors; (6) disposing of second-hand registers of the company's make with the object of underselling competitors and driving them from the business, provided that prices made in good faith to meet competition were not prohibited; (7) employing "competition men," whose principal business was to prevent sales of competing cash registers; (8) following from place to place competitors, their agents and dealers, with the design of hampering their sales; (9) circulating reports reflecting upon the solvency or responsibility of competitors or upon the efficiency of their machines, when such reports were spread as a means of preventing the

[1] The competitive methods of the company are described at considerable length in Petition in United States *v.* National Cash Register Company, December 4, 1911, pp. 12–29.

sales of competing registers; (10) intimidating competitors or intending competitors by displaying placards showing the sums lost by former competitors, or intimidating investors or prospective investors in competing enterprises; (11) threatening prospective purchasers of competing cash registers with suit for patent infringement, unless such claim of infringement had been sustained by a court of competent jurisdiction; (12) operating bogus independents; (13) acquiring ownership or control, directly or indirectly, of the business, patents, or plant of competitors; provided, that the court reserved jurisdiction to permit such acquisition, if it concluded, after investigation and on notice to the Attorney General, that the acquisition would supplement the facilities of the company, and would not substantially lessen competition in the industry.

The Court retained jurisdiction of the cause for the purpose of enforcing the decree, and of enabling the parties thereto to secure a modification thereof if it subsequently appeared that its provisions were inadequate to maintain competitive conditions, or were unduly oppressive to the company and were not necessary to maintain such competitive conditions.

The decree, it will be observed, did not require the dissolution of the trust. This is to be explained, no doubt, by the fact that the company made all of its machines at its plant in Dayton, Ohio; and there were therefore obvious difficulties in the way of a physical separation of parts of its business. It would have been possible, of course, to have segregated the various makes, yet this could hardly have been done without seriously interfering with the efficient conduct of the company's affairs. If we bear in mind the oppressive and illegal character of the company's acts through a period of some twenty years, it appears that the defendants had little occasion to complain of the treatment accorded them.

THE HARVESTER TRUST

The petition to dissolve the harvester trust was filed on April 30, 1912. This action had been preceded by several months of unsuccessful negotiations between the company and the

Department of Justice, looking toward a voluntary readjustment of the company's business. Subsequent to the bringing of this suit the company reorganized its affairs; and turned over its foreign business and the new lines to a new company,—the International Harvester Corporation.[1] The Department of Justice agreed with the Bureau of Corporations that this plan of disintegration did not suffice; and continued its suit.[2] On August 12, 1914, the Circuit Court rendered its decision, declaring the International Harvester Company a combination in restraint of trade among the states and with foreign nations.[3] In a decree filed on August 15 it ordered that the monopoly be forever dissolved, and that the business and assets of the company be divided "among at least three substantially equal, separate, distinct, and independent corporations, *with wholly separate owners and stockholders.*"[4] On October 3 the court agreed to modify the decree by striking out the words "with foreign nations" wherever they appeared, and by stipulating merely that the business and assets of the company be divided "in such manner and into such number of parts of separate and distinct ownership as may be necessary to restore competitive conditions and bring about a new situation in harmony with law."[5] The exact meaning of the decree as modified is not clear, but it is perhaps arguable that common stock ownership is also prohibited by the provision for dividing the business into "parts of separate and distinct ownership." The provision that the corporations among which the property of the trust was to be divided should have "separate owners and stockholders" was inserted at the request of the government; and was a recognition of the obvious fact that corporations having the same stockholders could hardly be expected to compete with one another. However, the gov-

[1] See p. 240.

[2] See p. 240. The attitude of the Attorney General is shown in Brief for the International Harvester Company (no. 757), p. 157.

[3] See p. 435.

[4] Decrees and Judgments in Federal Anti-Trust Cases, p. 338. Italics supplied by the author.

[5] Ibid., p. 340.

ernment agreed to the revised form of decree suggested by counsel for the trust.[1]

The International Harvester Company appealed from the decree of the Circuit Court to the Supreme Court. The case was there argued in April, 1915; reargued in March, 1917; and in May, 1917, was restored to the docket for further reargument. In January, 1918, reargument was deferred until the October term. This action was taken upon the request of the Attorney General, who stated that the dissolution of numerous trusts would require large financial operations, which should be avoided at that time in view of the situation created by the war.[2] Believing that a decision as to its legal status might be long delayed, and that meanwhile it would be unable because of the uncertainties of its position to prepare for the postwar competitive struggle, the company decided to withdraw its appeal, and to agree to a consent decree. An understanding was reached with the Department of Justice on July 11, 1918;[3] and in October, 1918, the Supreme Court dismissed the suit.

The agreement between the government and the company provided in substance:[4] (1) That the company would endeavor to sell at a fair price to a responsible and independent manufacturer of agricultural implements the lines of harvesting machines then marketed by it under the trade names of "Osborne," "Champion," and "Milwaukee," including their trade names and all equipment especially used for their manufacture. In the inability of the parties to agree on what constituted a fair price, the question should be settled by the District Court. (2) That the company would endeavor to sell in connection with said harvester lines the Osborne No. 1 plant at Auburn, N. Y., and the Champion harvester plant at Springfield, Ohio, under the same conditions as to price as enumerated above. (3) That the

[1] Decrees and Judgments in Federal Anti-Trust Cases, p. 339.

[2] Annual Report of the Attorney General, 1918, p. 62.

[3] Report of the Federal Trade Commission on the Causes of High Prices of Farm Implements, p. 658.

[4] A copy of the final decree, dated November 2, 1918, is in Report of the Federal Trade Commission on the Causes of High Prices of Farm Implements, pp. 710–713.

lines and plants mentioned above, if not sold within one year after the close of the war, should, upon request of the government, be disposed of at public auction to the highest bidder.[1] (4) That the company should be prohibited, after December 31, 1919, from having more than one representative or agent in any town in the United States to handle the sale of its harvesting machines and other agricultural implements. (5) That the object to be attained under the decree was to restore competitive conditions in harvesting machines and other agricultural implements; and if such competitive conditions had not been established within eighteen months after the expiration of the war,[2] the United States should have the right to such further relief as might be necessary.

Shortly after the agreement with the Department of Justice had been reached, the directors of the International Harvester Company (of New Jersey) and of the International Harvester Corporation, apparently with the approval of the Department, submitted to their stockholders a proposal for a merger of the two companies. The statement to the stockholders, dated August 10, 1918, pointed out that the International Harvester Company (of New Jersey) and the International Harvester Corporation had at no time been competitors, and had "maintained close and mutually beneficial trade relations." The Company manufactured only harvesting machinery, tillage implements, binder twine, and steel, and made no sales outside of the United States. The Corporation made the new lines (tractors, gas engines, etc.) in this country, operated the foreign plants formerly owned by the Company, and carried on the entire foreign trade in the products of both companies. However, the war had seriously crippled the business of the Corporation. In some countries its business had been curtailed, in others, notably Russia and the Central Empires, practically destroyed. Its

[1] In July, 1918, the Osborne line of harvesting machines was sold to the Emerson-Brantingham Company, and in December, 1918, the Champion line was sold to B. F. Avery and Sons, of Louisville, Ky. Ibid., pp. 660–661.

[2] Within two years from the date of the entry of the decree if the war should end within less than six months after the entry of the decree.

business in the new lines was excellent, but the Corporation was not sufficiently strong financially to develop these lines, or to compete actively for foreign trade upon the termination of the war. Since the Corporation distributed abroad the products of the Company, and the Company distributed in the United States the products of the Corporation, each had an interest in the prosperity of the other. Accordingly their reunion was recommended as essential to the efficient operation of the two companies.

The proposed merger was approved by the stockholders on September 10, 1918; and having received the approval of the New Jersey Utilities Commission went into effect on September 19, the name of the new company being the International Harvester Company.

How effective will the dissolution of the International Harvester Company prove? The Federal Trade Commission in a recent report on the Causes of High Prices of Farm Implements declared that the decree of the Court will fail in its purpose to restore competitive conditions in the harvesting machine business.[1] It based this conclusion upon the small and constantly declining output of the "Osborne," "Champion," and "Milwaukee" brands, as compared with the McCormick and Deering brands; upon the low factory costs of the McCormick and Deering brands as compared with the other brands, whether those to be disposed of by the International Harvester Company under the decree or those manufactured by independent companies; and upon the ownership by the International Harvester Company of the Wisconsin Steel Company. It therefore recommended that the decree be modified to provide (1) that the McCormick plant and brands and the Deering plant and brands should be owned by two separate companies; (2) that neither of these companies should be allowed to control the Wisconsin Steel Company;[2] and (3) that all three of these companies should have distinct and separate stockholders.

[1] See pp. 653–680.

[2] In this recommendation the Commission appears to have overstepped the mark; the integration of industry, which it proposed to forbid, is neither illegal nor opposed to sound economic policy.

THE GLUCOSE TRUST

The decision of the District Court dissolving the Corn Products Refining Company has been described elsewhere.[1] The decree of the court, entered on November 13, 1916, ordered the unlawful combination to be forever dissolved.[2] Following the precedent in the harvester case, the business of the company was to be divided "in such manner and into such parts of separate and distinct ownership" as might be necessary to restore competitive conditions. Finally, injunctions were issued against the use of a considerable number of unfair practices enumerated in the decree. The company appealed from the decree within the four months allowed to it, but subsequently, on March 31, 1919, withdrew its appeal, and accepted the terms proposed by the Department of Justice. The company took this action that it might be relieved of uncertainty, and might proceed, undisturbed by the fear of government prosecution, to make such improvements as would insure the future of its business.[3]

The settlement with the Department of Justice and the final decree of the district court—entered March 21, 1919—provided that the company before 1921 should sell its reserve plant at Davenport, Iowa, which had not been in operation for a number of years; its plant at Granite City, Illinois; and its securities in the National Starch Company and the Novelty Candy Company.[4] It further provided that these properties or securities should not be sold to a corporation or person controlled by or affiliated with the Refining Company, nor to any defendant in the suit; and that none of the directors, officers, or stockholders of the company should acquire a substantial interest in the corporation that purchased them. Moreover, the Corn Products Company and the purchaser might not have any directors or officers in common. If at the end of three years these measures

[1] See p. 436.

[2] A copy of the decree is in Judgments and Decrees in Federal Anti-Trust Cases, pp. 440–448.

[3] Letter of the president to the stockholders, April 25, 1919. Reprinted in Chron., 108, p. 1723.

[4] See Chron., 108, p. 1392.

proved inadequate, the government was to be permitted to have further relief.

The result of the decree was to leave the Corn Products Refining Company only three manufacturing plants, located at Argo and Pekin, Illinois, and Edgewater, New Jersey. The output of the Edgewater plant was largely marketed abroad, and the company had strongly protested against being forced to dispose of it. Its retention by the company leaves it in a position to compete effectively for the export trade.

THE MEAT COMBINATION

The leading meat-packers, united through pools or agreements of one kind or another during the past thirty years or more, have been attacked in numerous proceedings.[1] In 1902 the government filed a petition in equity against the leading packers, alleging a conspiracy to suppress competition and to obtain a monopoly in commerce in meats.[2] The Circuit Court granted a perpetual injunction in 1903, which was affirmed by the Supreme Court, with slight modification, in January, 1905.[3] The government maintained that the defendants continued to conduct their business in the manner forbidden by the injunction; and in July, 1905, an indictment was returned against practically the same defendants. The packers claimed that they were entitled to immunity from criminal prosecution because they had virtually been compelled to testify against themselves in connection with the investigation of the Bureau of Corporations into the beef industry; and they were sustained in this contention by the Court in a decision rendered in 1906.[4] This decision, which became known as the "immunity bath" decision, led to

[1] The nature of these pools and agreements, and the position of the leading packers in the industry, are described in the report of the Federal Trade Commission on the Meat-Packing Industry. The first three volumes of this report are summarized by the author in the American Economic Review, 9, pp. 880–885. See also the report of the Bureau of Corporations on the Beef Industry, March 3, 1905.

[2] Cf. p. 403.

[3] 122 Fed. Rep. 529; 196 U. S. 375.

[4] 142 Fed. Rep. 808.

congressional legislation whereby immunity from criminal prosecution was limited to natural persons giving testimony or evidence under oath in obedience to a subpœna.

In 1910 four new proceedings were instituted.[1] In March two suits—one civil and the other criminal—were brought against the National Packing Company, a concern organized in 1903 to hold certain independent properties that had been acquired by the Swift, Armour, and Morris companies in the interests of a merger that had been planned, but that failed to go through. The directors of the National Packing Company were all representatives of the three leading packers, and the company was used, it was alleged, as an agency for the harmonious determination of general policies and for the control of the trade. In April, 1910, a criminal action was brought against the Armour Packing Company; and in September one against Louis F. Swift and others. The civil suit against the National Packing Company was withdrawn to prevent the defendants from asking the Court for a postponement of the criminal proceedings until the settlement of the civil case; and all of the criminal suits were lost by the government. In 1912, possibly to avoid a new civil suit, the packers dissolved the National Packing Company, and distributed its assets among its owners, that is, among the Swift, Armour, and Morris interests.

Notwithstanding the claim of the Department of Justice that the dissolution of the National Packing Company accomplished a substantial restoration of competitive conditions,[2] the outcome of this large number of suits and the facts brought to light in later investigations, notably those of the Federal Trade Commission, made it clear that the activity of the government had availed comparatively little.

Much bids fair to be accomplished, however, by a recent court decree materially affecting the business of the leading packers known as the Big Five (Swift and Company, Armour and Company, Morris and Company, Wilson and Company, and Cudahy Packing Company). Influenced no doubt by the

[1] The Federal Antitrust Laws, July 1, 1916, pp. 62, 64.

[2] Annual Report of the Attorney General, 1912, p. 16.

prospect of regulative legislation directed particularly at the meat-packing industry, and by the imminence of a dissolution suit under the Sherman Act, the Big Five consented—so the Attorney General announced on December 18, 1919—to a decree that enjoined the practices of which the government had particularly complained.[1]

The decree of the Court was entered on February 27, 1920.[2] Legal verbiage omitted, it provided as follows:

(1) The corporate defendants were perpetually enjoined from maintaining in any manner any contract or combination in restraint of interstate commerce, and from monopolizing any part of such commerce (sec. 1).

(2) The defendants (individual and corporate) were perpetually enjoined from owning, directly or indirectly, any capital stock or other interest in any public stockyard market company in the United States, or in any stockyard terminal railroad in the United States, or in any stockyard market newspaper or journal published in the United States (sec. 2). The defendants within ninety days after the entry of the decree were to file with the Court, for its approval, their plan for divesting themselves of all ownership or interest in these facilities, whereupon the Court, if it approved the plan, was to determine the date by which it should be carried out (sec. 10). The purchasers of the defendants' interests in stockyards were to agree with such of the defendants as then maintained packing plants in these stockyards that for a period of ten years the former should continue to operate the stockyards efficiently, and the latter should continue to operate the packing plants, unless strikes or other causes beyond their control should prevent (sec. 13).

(3) The corporate defendants were perpetually enjoined from using their distributive system and facilities, including their

[1] These practices are briefly described in the petition for the United States in United States v. Swift and Company et al. (no. 37623); and in detail in the report of the Federal Trade Commission on the Meat-Packing Industry (see particularly the summary in part I, pp. 28–78).

[2] A copy is in Decrees and Consents, Petition, Answers, and Stipulation in United States v. Swift and Company (no. 37623), a pamphlet published by the Department of Justice.

branch houses, route cars, and auto trucks, in the handling of a large number of articles enumerated in section four, except in so far as permitted in that section, and except refrigerator cars when in good faith leased to common carriers. The defendants might dispose of any part of their distributive system with the approval of the Court (sec. 3).

(4) The corporate defendants were perpetually enjoined from carrying on in the United States, directly or indirectly, either for domestic trade or export trade, the manufacturing, jobbing, selling, transporting (except as common carriers), distributing, or otherwise dealing in a large number of commodities, including, among others, fish, vegetables, fruits, confectionery, soft drinks, preserves of all kinds, spices and relishes, coffee, tea, chocolate, cocoa, nuts, flour, sugar, rice, bread and crackers, cereals, grain, grape juice, and miscellaneous articles. Provided, however, that these commodities might be dealt in by the defendants when used (a) as supplies in operating their packing plants, branch houses, and other facilities; (b) in the construction and physical maintenance of their packing houses and other facilities; (c) in the operation of their restaurants, laundries, or other conveniences; or (d) in combination with meat (sec. 4). The requirements of this section were to be met at as early a date as possible, but in no event to be delayed beyond two years from the entry of the decree. The approval of the Court to the final disposition was required, and the Attorney General at any time within the two year period might apply to the Court for an order compelling the defendants to make a report of progress (sec. 12).

(5) The individual defendants were perpetually enjoined from owning, either directly or indirectly, voting stock which in the aggregate amounted to 50 per cent or more of the voting stock of any corporation (except common carriers), or from holding a half interest or more in any firm, which was carrying on in the United States the business of manufacturing, jobbing, selling, transporting, or distributing a large number of commodities, including all those enumerated in the preceding section except cereals, grain, grape juice, and miscellaneous articles

(sec. 5). As with the corporate defendants the provisions of this section were to be fully met within two years at the outside (sec. 12).

(6) The defendants were perpetually enjoined from owning or operating in the United States, either directly or indirectly, any retail meat markets, except those located at their plants and maintained primarily for the accommodation of their own employees (sec. 6).

(7) The defendants were perpetually enjoined from owning, directly or indirectly, any capital stock or other interest in public cold-storage warehouses in the United States, subject to certain exceptions (sec. 7). Immediately upon the entry of the decree the defendants were to proceed with due diligence to divest themselves (to the extent required by the decree) of their retail meat markets and their public cold-storage warehouses, but the approval of the Court to such disposition must be had. At the end of nine months, if these interests had not all been disposed of, the Attorney General might apply to the Court for an order specifying the date by which the transactions should be completed (sec. 11).

(8) The corporate defendants were perpetually enjoined from engaging in the United States, either directly or indirectly, in the business of buying, selling, or dealing in fresh milk and cream, except when the milk or cream constituted the raw materials for certain commodities the manufacture of which was permitted to them, and except when their sale was necessary to avoid waste (sec. 8).

(9) The corporate defendants were perpetually enjoined from employing any illegal trade practices (sec. 9).

(10) For the purpose of enabling the government to ascertain whether the defendants were carrying out the terms of the decree in good faith, the corporate defendants were directed to submit their books, records, correspondence, and other documents to the Attorney General upon his meeting certain requirements, such as written notice of alleged violations, and the like (sec. 16).

(11) Jurisdiction of the cause was retained by the Court for

the purpose of adding such further relief as might become necessary for the enforcement of the decree (sec. 18).

From this brief recital of the terms of the decree it is evident that the dissolution of the beef combination—a combination that threatened, according to the Federal Trade Commission, to control within a few years the wholesale distribution of the nation's food supply—was unusually far-reaching in character. It remains to be seen whether its effect will be to restore competition among the packers in the production of meat and allied products.

THE STEEL TRUST

A petition to dissolve the steel trust was filed on October 27, 1911. The District Court rendered a decision in favor of the Corporation on June 3, 1915, and the Supreme Court affirmed the verdict on March 1, 1920.[1] The outcome of the suit against this mammoth organization is highly significant in its bearing on the effectiveness of dissolution proceedings as a means of solving the trust problem.

CONSENT DECREES

The foregoing dissolution proceedings deal with trusts that at one stage or another have contested the suits brought against them. Yet in numerous instances the government has been able to secure relief without legal contest; the companies attacked by the government have been unwilling to fight the case, and have consented to a decree. In very few instances, if any, have these consent decrees involved the physical division of the plants or assets of the companies. Instead they have dealt rather with the future conduct of the trust or combination.

One of the trusts that accepted a consent decree was the Aluminum Company of America. The government instituted suit against this company on May 16, 1912. It charged[2] that the Aluminum Company of America had been protected against competition by patents down to 1909, and that thereafter it had endeavored to maintain its monopolistic position by controlling,

[1] Cf. p. 438.

[2] Petition in United States *v.* Aluminum Company of America, pp. 1–43.

either through purchase or agreements, the essential raw materials, and by employing unfair methods of competition against its would-be rivals.

The basis of the aluminum industry is bauxite, a crude ore found in extensive natural deposits. The bauxite is refined into alumina, from which the metal aluminum is made. The Aluminum Company prior to the date of the government suit made large purchases of bauxite properties, and entered into contracts with other concerns, whereby they agreed not to use their bauxite deposits in the manufacture of aluminum, nor to sell them for such purpose to any one but the Aluminum Company of America. The latter entered into an international pooling arrangement with the Neuhausen Company, the largest European producer of aluminum, whereunder the European company agreed not to sell aluminum in the United States. Being almost the sole source of supply of aluminum metal the Aluminum Company was in a position to monopolize the manufacture of aluminum goods, such as cooking utensils, castings, novelties, etc.; and according to the government the company through the use of unfair competitive tactics was rapidly extending its control in these branches. The unfair acts complained of included among others: refusal to supply independent manufacturers with the necessary aluminum metal, often without warning or explanation; purposeful delaying of bills of lading on material shipped to competitors; refusal to guarantee quality, and delivery of defective metal; and charging of higher prices on aluminum sold to competitors than to companies in which the Aluminum Company was interested.

The decree of the Court granted on June 7, 1912, declared the agreements with the Neuhausen Company and the American companies to be null and void, and perpetually enjoined the making of any like agreements.[1] It also forbade the defendant and its officers and agents ever to enter into any combination or agreement the purpose or effect of which was to control the output or the prices of aluminum or its raw materials, and to enter into any contract or agreement the effect of which was to restrain

[1] Decrees and Judgments in Federal Anti-Trust Cases, p. 341.

commerce in bauxite, alumina, or aluminum, or to hinder anyone in obtaining a supply of such articles in the open market in free and fair competition. It further perpetually enjoined the employment by the defendant of the unfair practices referred to above. The decree being agreed to by the Alunimum Company of America on the assumption that it had a substantial monopoly of the output and sale of aluminum in this country, it was further provided that whenever it should appear to the Court that substantial competition in the production and sale of aluminum in this country had arisen, the Court upon petition might modify the decree.

Other leading companies—trusts or important combinations—that have submitted to consent decrees are: American Coal Products Company;[1] American Thread Company;[2] S. F. Bowser and Company (a combination in pumps, tanks, and outfits used for the storage and handling of gasoline and other inflammable liquids);[3] Burroughs Adding Machine Company;[4] Central West Publishing Company (with the Western Newspaper Union substantially the sole manufacturer of ready-print newspaper matter);[5] General Electric Company;[6] and Otis Elevator Company.[7] Many other companies have consented to decrees, but these are the principal ones. In no instance were the aforementioned companies required to submit to a physical dissolution; the decree merely enjoined certain objectionable practices, though in a few instances it ordered the dissolution of a few subsidiary companies or the sale of some securities.

In addition a number of associations in restraint of trade have yielded to consent decrees. Among them are the Automobile Bumper Association,[8] the New Departure Manufacturing Company and others (manufacturers of bicycle and motor-cycle coaster brakes and parts),[9] the News-Print Manufacturers' Association,[10] and the Southern Wholesale Grocers' Association.[11]

[1] Decrees and Judgments in Federal Anti-Trust Cases, pp. 461–467.
[2] Ibid., pp. 449–456.
[3] Ibid., pp. 587–592.
[4] Ibid., pp. 457–459.
[5] Ibid., pp. 359–371.
[6] Ibid., pp. 267–273.
[7] Ibid., pp. 107–113.
[8] Ibid., pp. 645–648.
[9] Ibid., pp. 471–475.
[10] Ibid., pp. 637–640.
[11] Ibid., pp. 247–251, 802–803.

Against a number of important trusts and leading combinations suits are now [1] pending. The more important cases are those against the American Can Company, the American Sugar Refining Company, the Eastman Kodak Company, and the Keystone Watch Case Company. The decision of the lower court has been rendered in all of these cases, except in that against the American Sugar Refining Company. The verdict was for the government in the Kodak case, and partly for it and partly against it in the Keystone case. In the Can case the trust was declared to have been organized as an unlawful combination, but the only relief granted was the retention of the bill, that is, the maintenance of court supervision over the company, with power granted to the government to show to the Court at any time, if it could, that the company was using its power to the injury of the public, or that the domination of the company over the industry was so great as to justify dissolution. Appeals in these cases are now pending in the Supreme Court. It is a striking illustration of the law's delays, that though the suit against the American Sugar Refining Company was instituted in November, 1910, a decision by the lower court has not yet been rendered. The case was ready for trial in October, 1915, but the Court ordered the hearing postponed pending the decisions of the Supreme Court in the harvester and steel suits.[2] The former has now been withdrawn from the Court's docket, and the latter after being postponed from time to time has been decided in favor of the company. A partial explanation of the delay in the disposition of the steel case is that the Attorney General on January 2, 1918, asked the Supreme Court to defer argument on this and several other anti-trust suits until the fall term of the Court.[3] Meanwhile ten years have elapsed since the suit against the sugar trust was first brought.

From the foregoing record it is clear that the program of

[1] November, 1920.

[2] Annual Report of the Attorney General, 1916, p. 28.

[3] Chron., 106, p. 32. It is only fair to the United States Steel Corporation to say that this suspension was opposed by it.

trust dissolution has by no means been fully successful. How is this comparative lack of success to be explained?

One of the principal explanations is the failure to prohibit the companies among which the property of the trust was divided from having substantially the same stockholders. The first trusts to be dissolved were the oil and the tobacco trusts. The Supreme Court had found these trusts clearly illegal under any interpretation of the Sherman Act, and had arraigned them severely because of their competitive tactics. Nevertheless the dissolution decrees in these two cases were totally inadequate to restore competitive conditions. Such an unfavorable outcome, indeed, was all that could have been expected of a dissolution that permitted the majority stockholders of each of these trusts to exercise control over the separate companies into which each was split. This was the view taken by the Federal Trade Commission, which investigated the results of the Standard Oil dissolution. The Commission, though it refrained from criticising the decree itself, partly because it was to be regarded as an experiment, nevertheless expressed its opinion, after mature deliberation, that the experiment of dissolving corporations without separating owners had not achieved the desired purpose, which was the establishment of effective competition.[1] The decree in the oil case, moreover, was notably lacking in those injunctive provisions that characterized later decrees of the courts. The decree in the tobacco case was more complete, both in the details of dissolution and in the restrictions on the future activities of the tobacco companies, but as pointed out before at much length it was open to criticism at many points. As in the oil case, the fourteen tobacco corporations that took over the business of the trust were permitted to have common stockholders. It was our experience with these trusts that induced President Wilson in his message on trust legislation in 1914 to present to Congress for its consideration the advisability of requiring individuals owning stock in companies which ought to be independent, but which because of common stockownership were not, to choose in which one of them they would elect the right to vote. This suggestion,

[1] See p. 451.

which went to the heart of the matter, was not heeded by Congress, which failed to act, no doubt, on the ground that individuals were privileged to hold what stocks they chose. Within a few months after the delivery of the President's message, a district court provided for the distribution of the business of the International Harvester Company among at least three substantially equal, separate, distinct, and independent corporations, *with wholly separate owners and stockholders*, but some six weeks later with the consent of the Attorney General this provision was struck out.[1] A similar provision is found, so far as we have been able to discover, in only two other court decrees.[2] Another explanation of this lack of success is the ineffective manner in which the prosecutions have been conducted, particularly during the early life of the law. The first trust cases were lost because of faulty presentation [3] or because of the failure of the Attorney General to press them to a conclusion.[4] A number of others were not brought until long after the organization of the several trusts, for the reason that the officials charged with the enforcement of the Sherman Act had no sympathy with its purposes. Moreover, the frequent changes in administration —the period of service of an attorney general has averaged about two years—have led to varying policies, and have therefore not promoted the effective handling of trust cases.

A third explanation is the failure to recognize sufficiently that dissolution is not only a legal problem, but an economic one as well. This was conceded by the Attorney General in connection with the tobacco trust case. Yet in this very case the lower court waved aside certain objections that bore on the "economics" of the tobacco business, saying, "no doubt the novel problem presented to this court is connected with questions of economics as well as with questions of law. But

[1] See p. 480.

[2] The glucose (see p. 484) and the Eastman Kodak (see Decrees and Judgments in Federal Anti-Trust Cases, p. 478). An appeal is pending in the latter case.

[3] Cf. pp. 441, 442.

[4] Cf. p. 442.

this is a court of law, not a commerce commission, and the legal side of the proposition would seem to be the controlling one." [1] In order that expert knowledge as to economic matters might be available for the courts, Congress provided in 1914 that the Federal Trade Commission, at the request of any court, should frame an appropriate form of decree in any suit in equity brought by the Attorney General under the anti-trust acts. Doubtless Congress intended that the courts should avail themselves of this privilege, but they have rarely done so, and on one occasion they actually denied a request of the defendant that the plan of dissolution be framed by the Commission.

A fourth explanation is the failure of the courts and juries to impose penalties proportionate to the offense committed. The government has brought both criminal and civil actions. In the former, prison sentences have rarely been imposed, and fines have been very light, often much less than the illegal profits realized. The law not being fully clarified, juries have hesitated to convict when the penalty was to be imprisonment. No doubt this was proper during the early stages of the enforcement of the law; if the government was unable to define the offense with precision, or was not able to advise the parties as to just what was legal and what was not, the justice of sending to jail those who crossed an undefinable line was doubtful. Looking into the future, however, as the anti-trust laws receive fuller interpretation at the hands of the courts, so that business men are in a better position to know definitely what is legal and what is illegal, it may perhaps be anticipated that less leniency will be shown law breakers. The adoption of a code of business ethics through the activities of the Federal Trade Commission under its powers to prevent unfair methods of competition should also operate towards the same end. It may be, therefore, that the penal laws will become more effective in the future than they have been in the past.

In the civil cases the government has been more successful. Approximately one hundred suits in equity of varying degrees of importance have been brought under the Sherman Act, and

[1] See p. 467.

the government has won a considerable proportion of them. In a number of instances, as related above, the offending corporations have not even contested the case, but simultaneously with the filing of the suit have consented to a court decree granting the relief demanded by the government. The successful outcome of these suits has been due to the fact that the proceedings were remedial, rather than punitive, penalties applying only when the decree of the court was disobeyed. It is thus the equity feature of the Sherman Act that has given it a large part of such effectiveness as it has had in the past. However, a statute that does not include within its prohibitions a combination of the size and power of the United States Steel Corporation must be conceded to be of limited effectiveness.

It would be a mistake, however, to judge of the success of the Sherman Act solely by the readjustments that have been brought about through judicial proceedings. The mere existence of the act and the possibility of prosecution under it have reduced the necessity for its exercise, just as the conferring on the Federal Trade Commission of the power to prevent unfair methods of competition has given it less occasion to use that power. It is worthy of note that practically no new trusts have been formed since the government energetically began to avail itself of the provisions of the anti-trust acts, and that many of those already organized have been less active in maintaining their position by unfair means. Some of our modern trusts, notably the harvester, can, sugar, and steel trusts, have so revised their practices that their competitors find little cause to complain of their conduct. Doubtless the managers of the modern day trusts believe that it pays to cultivate the good will of the public, but is this not in large measure because of the fact that the public (through its constituted authority) has readily at hand the tools with which to proceed against these trusts, once its hostility is fully aroused? We have but to call to mind the threat of governmental control of the meat-packing industry, and the decision of the packers to submit to a consent decree by way of bending to the storm. And if the courts retain jurisdiction of trust cases after a decree has been entered, as they did in the powder, cash

register, harvester, glucose, meat, lamp, and can cases, for the purpose of modifying the decree if the provisions thereof prove inadequate, there is greater cause to anticipate success in the restoration of competition. The significance of this recent tendency becomes clearer when it is recalled that in the tobacco case the Attorney General had asked the Court to reserve to the government the privilege of applying for further relief, if during the following five years it appeared that the dissolution plan had not brought about a situation in harmony with the law; and that the Court held (in 1911) that it had no such power. Now it appears that the Courts do have such power, and are ready to exercise it if necessary to carry out the purpose of the statute.

CHAPTER XIX

THE ANTICIPATED ECONOMIES OF THE TRUST FORM OF ORGANIZATION—TO WHAT EXTENT REALIZED [1]

There seems little reason to doubt that the modern trust movement originated largely in the desire of the manufacturers to restrict or suppress competition, and thus to secure monopoly profits. Nevertheless the prospect of securing the economies that the trust form of organization apparently promised also played a considerable part. It is the purpose of this chapter to consider in some detail whether these economies, as realized in practice, are of sufficient importance from the standpoint of public welfare to justify trusts, it being assumed that through government regulation it will be possible to control these huge organizations in so far as this seems necessary or desirable. In other words, is the policy of trust dissolution ill-advised, as occasioning the destruction of an organization superior in efficiency to the one it was intended to replace?

In this discussion it is important that the reader keep clearly in mind the meaning of the word trust as it was defined in the beginning of the book.[2] The trust, tersely stated, is a horizontal combination possessing monopolistic power. The economies of the trust form of organization must at all times be clearly distinguished, first, from the economies of *large-scale* production, and second, from the economies that may be realized by a *combination* not possessing monopolistic power. The trust, it would seem, should receive legal sanction only if it is able with-

[1] See Bullock, Quarterly Journal of Economics, 15, pp. 167–217; Durand, The Trust Problem, ch. 4; Jenks and Clark, The Trust Problem, ch. 3; Montague, Trusts of To-Day, ch. 2; Ely, Monopolies and Trusts, ch. 4; and Industrial Commission, vols. 1 and 13.

[2] See p. 1.

out injury to the public welfare to reduce the costs of production or of selling in ways that are not open to large individual plants, and in ways, moreover, that are not open to a combination of large (or small) plants that has no monopolistic power. In some branches of industry, it is to be observed, it may be possible to unite fifty or more plants without achieving a dominant position in the industry. Obviously, therefore, the economies that may fairly be ascribed to the trust are solely those *additional* economies that a large-sized combination not holding a preponderant position in the industry is unable to secure.

The economies of the trust form of organization may be analyzed under three heads:

I. Economies in Bargaining.
II. Economies in Production.
III. Economies in Selling.

I. *Economies in Bargaining*

The economies in bargaining may be treated under the following headings: (1) purchase of materials and supplies; (2) distributors; (3) labor; (4) financial institutions; (5) railroads.

(1) Purchase of materials and supplies. Large concerns, of course, can often buy their raw materials and supplies more cheaply than small concerns, but can a trust buy its materials more cheaply than a large-sized combination? Viewed in one light the trust can more or less permanently secure its raw materials more cheaply than would be possible under a state of competition. The monopoly profits of the trust arise largely from a restriction of the output,[1] and this necessarily involves a reduction of the demand for the raw materials consumed by it. If the raw materials required by the trust are used in many other industries, as is the case with the tin plate trust, for example, the reduction in the price of the raw materials may be slight; if they are used in practically no other industry, as is the case with the tobacco trust, the reduction may be considerable. The

[1] If the trust is actually more efficient than other business units, it can of course secure monopoly profits without restricting the output, by merely appropriating the savings effected by it.

tendency toward a reduction in the price of the materials and supplies is accentuated if the industry is one of increasing costs, and attenuated if it is one of decreasing costs. However, the attainment in this way of a lower price level for materials confers no advantage upon the trust as compared with its competitors; and is hardly to be cited as an argument for the trust form of organization, since the result is a diminution in the wealth of the country, both in terms of raw materials and of finished products.

Without reducing its own output, the trust may nevertheless succeed in depressing the market for materials and supplies, providing, of course, it is not confronted with a trust in these lines. If the sellers of leaf tobacco, for example, had reason to believe that there would be a market for their total output, they would normally be inclined to withhold their product until they had secured the price determined by the equilibrium of demand and supply. But since the demand is uncertain—it depends, of course, largely on the amount the trust decides to buy—they may be tempted, particularly since many of them can not afford to hold their crop indefinitely, to take a lower price in order to make sure of a sale.[1] If the lower market price thus registered is open to the competitors of the trust, they gain equally with it; yet in either event this economy in the purchase of raw material represents no social benefit, since the producers lose what the trust gains. This practice persistently employed will therefore tend to discourage the production of the articles used by the trust, and thus to diminish national wealth.

There is one direction in which trusts may perhaps gain. If they can eliminate unnecessary middlemen, that is, promote a more direct and economical distribution of raw materials and supplies from the producer to themselves (the trusts), they will reduce costs, and in addition will be performing a real public service. And yet the trust may not have any particular advantage in this respect over the large combination; for the advantages of wholesale buying do not increase indefinitely.

[1] If their product is perishable, the position of the sellers is even more unfortunate.

The president of the American Tobacco Company, while claiming some advantage in the purchase of labels and similar articles, admitted that the trust could not buy the principal raw materials—leaf tobacco, sugar, and licorice—any cheaper than its competitors; in fact, it was at somewhat of a disadvantage, since it could not pick up bargains in the same way that a smaller buyer could.[1] Testimony to the same effect was given by the promoter of the rubber trust; by a leading official in the Standard Rope and Twine Company (a successor of the cordage trust); and by the president of the silver-ware trust.[2] A competitor of the whisky trust asserted that he could buy one car of corn just as cheaply as the trust could buy 100,000 bushels (say 80 cars);[3] and counsel for the Corn Products Refining Company (the glucose trust) admitted that his company had no advantage in the purchase of corn.[4] The president of the United States Steel Corporation testified that the constituent companies of the trust each purchased their supplies separately,[5] thus showing that the formation of a trust did not permit any saving in this regard. The conclusion would appear to be justified that while trusts may have decided advantages in buying as compared with small concerns, they have no striking advantages, if any, over large companies, except indeed such advantages as represent no social benefit.

The trust, to be sure, can often effect a saving by integrating its business in such a way that it assures itself an ample supply of raw materials at cost; and it is the more likely to find this advantageous, if it must buy its raw materials from another trust further down in the productive process. Yet integration is not limited to the trust form of organization; it is open to any concern with ample financial resources and operating on a large enough scale to justify the undertaking. The Bethlehem Steel Corporation, for example, is as fully integrated as the United

[1] Industrial Commission, XIII, pp. 326–327.

[2] Ibid., p. 36; I, pp. 163, 1050.

[3] Ibid., I, p. 184.

[4] Brief for the Corn Products Refining Company (no. 10–122), p. 31.

[5] Industrial Commission, XIII, p. 453.

States Steel Corporation. If integration is incomplete, so that the trust must still rely on other concerns for a portion of its materials, the production of a part of its supply may improve its strategic position, and may result in an economy in bargaining; if, on the other hand, integration is complete, the absorption by the trust of the profit at all stages of the productive process represents an economy in production. Yet in either event, whether the economy be one of bargaining or of production, the gain accrues, not as the result of the organization of a trust, but as a result of the integration of industry,—a practice that may be availed of by any concern, whether trust or not, which produces on a sufficiently large scale and which is able to command the requisite capital.

(2) Distributors. The trust is unquestionably in a position to bargain more effectively with the distributors of its products. The trust, controlling the greater part of the supply of a particular commodity, naturally possesses a strategic position in negotiations with the distributors, whether they be jobbers, wholesalers, or even retailers. The evidence indicates that the tobacco trust, for example, was able to encroach steadily on the jobbers' margins during the period from 1901 to 1910.[1] To the extent that the competitive system had evolved a distributing organization that was wasteful, there would be an obvious gain in the reduction of the number of distributors. However, the available information does not indicate that the formation of trusts has been accompanied by far-reaching changes in the distributive machinery. The wall paper trust endeavored to economize by eliminating the middleman, but after three years gave up the experiment.[2] There are lines of business, to be sure, in which the middlemen have been eliminated in the selling end, yet these are not solely or characteristically those businesses that are dominated by trusts.

[1] Report of the Commissioner of Corporations on the Tobacco Industry, part III, pp. 71, 80, 171, 190.

[2] Industrial Commission, XIII, p. 284. The cotton yarn trust endeavored to dispense with the services of the commission merchants who were accustomed to handle the sales of cotton yarn on a commission basis; but lost more

The trust, it must be admitted, sometimes took advantage of the power over the distributors that its control of the trade gave it. As Mr. Montague says, "in some manner or other, every trust seeks to dominate the wholesale trade." [1] The most common practice was a requirement that the wholesaler (and perhaps retailer also) handle only the goods produced by the trust, this requirement being reënforced ordinarily by a rebate for the faithful observance of the restriction. These factors' agreements were employed by many trusts, including the tobacco, rubber, sugar, whisky, wall paper, tin plate, photographic camera, and plate glass trusts. Such devices, of course, are not justified from an economic point of view; and they are now illegal.

(3) Labor. The trust may be said to have an advantage in its dealings with labor. Thus, during 1899 the American Smelting and Refining Company, confronted with a strike at its Colorado plant, suspended operations there, but continued to produce at its other plants.[2] The trust sustained a comparatively small loss through the idleness of the smelter, whereas the workmen sustained a heavy loss; and as a result the strike was a failure. Within limits, of course, this method of handling labor difficulties may be employed by a combination, as well as by a trust. Yet whether employed by combination or trust, its effectiveness depends on the lack of organization among the workers. If the organization of trusts reduced the bargaining power of labor, as it undoubtedly did, it demonstrated to the workers that they must make their organizations fully as broad in scope as the agencies with which they had to bargain. The gain of the trusts on this score may therefore prove to be temporary, particularly should the workingman come to realize more and more the advantage to his group of effective organization and unity of action.

by the change than it gained. See Dewing, Corporate Promotions and Reorganizations, p. 322.

[1] Trusts of To-Day, p. 44.

[2] The sugar trust had similar success in 1910 with a strike at its Brooklyn refinery. See Hearings on the American Sugar Refining Company, 1911–1912, p. 2994.

(4) Financial institutions. The trust, by virtue of the monopoly strength of the organization and the financial standing of its directors, can possibly borrow from the banks at lower rates of interest than can other concerns. This may be true, though, if it be true, it is a serious indictment of our banking system; and the advantage thus gained may be deemed to be a temporary as well as a nonsocial one. The probability, however, is that it is not true under normal conditions; the large concern with a stable and solvent business and high grade management, not to mention a combination of this character, can ordinarily borrow as cheaply as the more powerful trust. Under certain circumstances, to be sure, banks controlled by individual trusts or their stockholders may deny much needed credit to a competitor for the purpose of throttling it. This practice was presumably resorted to by the United Shoe Machinery Corporation to prevent a competing line of shoe machinery being established.[1] Yet obviously the successful employment of such practices does not establish the ability of a trust to borrow more cheaply than a combination could in the absence of such an obstructive trust.

A trust can sell its securities to the public (through investment houses perhaps) at better prices because of the wide distribution of its business, yet the saving that it can realize in this regard as compared with an important combination is slight, and would not appreciably affect the total cost of doing business. Many concerns do not appeal to the public for funds, but finance themselves out of surplus earnings.

(5) Railroads. Trusts, it may plausibly be asserted, are in a position to negotiate effectively with railroads and other transportation agencies, and by reason of the large traffic that they control to secure concessions in rates and facilities. Unfortunately in the past this has been altogether too true; the oil trust stands out as a shining example of the iniquities of railroad dis-

[1] See testimony of Mr. (now Justice) Louis D. Brandeis in Report of the Senate Committee on Interstate Commerce on Control of Corporations, 1913, pp. 1188–1190. Even more improper was the device employed by the American Sugar Refining Company to prevent a newly constructed independent refinery from being operated. See p. 101.

crimination. Such practices, however, offend the rules of fair play, and stand condemned at the bar of public opinion. Their importance has diminished, and will doubtless continue to diminish.

II. *Economies in Production*

The economies in production fall in the following groups: (1) continuous operation of plants; (2) specialization of plants and machinery; (3) specialization of ability; (4) employment in each plant of the best devices, including patents; (5) competition between plants; (6) utilization of by-products; (7) insurance; (8) smaller fixed charges per unit of product.

(1) Continuous operation of plants. Under competitive conditions the producing capacity of the country frequently exceeds the demand at prices remunerative to producers, and as a result there is some idle equipment.[1] The trust can correct this situation, it is thought, by closing the inefficient and poorly located plants, and by operating the better ones at capacity. It is obvious that the trust may take such action, though it is equally clear that the result is often a diminution in the output. It is difficult to determine the amount of the saving that the trust can effect in this way, but it is probable that it is less than is claimed. The increase in plant capacity in manufactures ordinarily comes through the provision of a number of new plants (or additions to old ones), no one of which produces more than a small percentage of the total output. There are, to be sure, a few industries in which a single factory will produce a large proportion of the country's output, yet this is the exception rather than the rule. Why, it may be asked, are so many new plants built, if the result is an excess capacity? There are two obvious explanations.

First, the construction of new factories may be in anticipation of an increase in demand which will shortly cause the surplus capacity to disappear and permit the properties to realize a satisfactory profit. In the United States, where most industries show

[1] This sometimes results from governmental tinkering. See Bullock, Quarterly Journal of Economics, 15, pp. 194–195, 208–210.

a more or less steady growth, this outcome is regularly to be expected, though the probability of continued growth leads to the provision of still further plant facilities which sooner or later run ahead of the demand. Our rapid growth is thus in considerable measure responsible for the imperfections of our competitive system. However, even the trust must possess some surplus producing capacity at all times except those of maximum demand, if it is to be in a position to supply the increased demand when it comes. This is particularly true in those branches of industry in which the adjustment of supply to demand is most imperfect, since it is in these branches—iron and steel, for example—that the length of time required to construct new plants is ordinarily greatest.

Second, the price may be sufficiently high, despite the excessive facilities, to attract those entrepreneurs of unusual ability who, by virtue of low costs, can make a profit when the extra-marginal producers are unable to do so. If the prospective demand does materialize, the market may temporarily absorb the total supply, including that of the relatively inefficient producers. Yet the time will come sooner or later when it will fail to do this; and then there must be a reckoning. Under competitive conditions the reckoning will normally take the form of the elimination of the high cost concerns. By this process then the surplus producing capacity tends to disappear, though so long as industry continues to be characterized by alternations of prosperity and depression it will not permanently disappear.

In what way can the trust improve on this operation of competitive forces? First, the trust by buying up the inefficient plants can close them more promptly than would otherwise occur. Yet this is subject to the danger that it will shut up so many plants that there will eventuate an undue limitation of the supply (in order that monopoly prices may be realized); and this would mean that the public would be obliged permanently to pay for the monopolized commodity a price sufficiently high to cover a return on the investment in inefficient and not to be utilized plants.[1] It is probable, therefore, that the public inter-

[1] Assuming that the trust retains its monopolistic power.

est would be better served by a combination uniting a limited number of the most efficient plants than it would be by a trust, which must acquire the inefficient plants as well as the efficient if it is to succeed in its monopolistic purpose. Second, the trust through its control of the supply may conceivably so adjust the output to the varying demand that an excessive producing capacity will not again emerge. This is conceivable, but hardly probable. Despite the establishment of trusts on a large scale some twenty or more years ago there continue to be pronounced oscillations of business. The United States Steel Corporation, our largest industrial concern, organized in an industry notable for its fluctuations, has endeavored to justify itself by introducing a new order in this respect, yet without conspicuous success. Unquestionably it has somewhat reduced the irregularity of business, yet at the present writing [1] it is able to produce about twice as much steel as it is in fact producing. The truth would appear to be that it is impossible, unless indeed under a socialistic state, satisfactorily and at all times to synchronize the supply and demand; and it would manifestly be difficult, if not impossible, even under a socialist state because of the impossibility of controlling the weather, the discovery of minerals, and the whims of a fickle public.

Conceding that alternations of boom and depression are inevitable in the system of private property it may be held that there is still an advantage for the trust, in that in periods of depression it can operate a part of its plants at capacity with a consequent reduction in their costs, and can close the other plants entirely. Thus, the American Sugar Refining Company adopted the practice of running most of its refineries at capacity at all times, and of adjusting the supply of its product to the demand by changes in the output of the Brooklyn refinery, its largest and best equipped factory. In this way the trust confined the higher cost that results from operation at partial capacity to one plant, producing a comparatively small percentage of its total output, whereas its competitors sustained this higher cost on their total investment, provided none of them had more than

[1] May, 1919.

one refinery. Mr. Havemeyer, formerly the head of the sugar trust, was of the opinion that in this direction his company effected its greatest saving. However, with respect to this economy the following observations may be made: (1) this arrangement may be adopted by a combination as well as by a trust, though no doubt the former would not be able to run as large a percentage of its plants at capacity; (2) it represents a gain only during those periods when some idleness is enforced by a diminished demand; (3) it is not possible in every industry, for in some industries all of the factories are perforce idle during a part of the year; [1] (4) it is not feasible when the trust has specialized its plants; (5) in some instances it may be more economical to operate at partial capacity than to pay the freight rate from the factory that is used as a buffer,—notably true when the plants have been located with the design of reducing cross freights, and when the freight rate constitutes an important item in the cost.

(2) Specialization of plants and machinery. The trust can specialize its plants, and thus secure the higher degree of efficiency that ordinarily results from specialization. The stock illustration of this saving is the American Steel Hoop Company, a manufacturer of iron and steel hoops, bands, bars, and cotton ties, all of which are rolled on high speed rolls. Prior to the organization of the trust each plant manufactured a great variety of shapes and sizes, and consequently had to keep on hand a great variety of rolls. Much time was necessarily lost in changing the rolls to meet the demand for the various sizes. With the organization of the trust it became possible for each mill to specialize more or less on particular shapes and sizes, and thus to eliminate much of the waste effort.

While it is true that there is the possibility of economy in this direction, its importance should not be exaggerated. Thus one writer states that the steel hoop trust as the result of specializing its plants effected a saving in manufacture estimated at $1.00 to $1.50 per ton as compared with the competitive system,

[1] Beet sugar factories are idle about two-thirds of the year. See Report of the Federal Trade Commission on the Beet Sugar Industry, p. 2.

or the system of small independent mills. This comparison, however, is hardly fair; for obviously in estimating the savings effected by the trust, comparison should not be made with small mills, but with mills of the size of those that were combined in the trust. The mere fact of having joined the trust did not, of course, by a stroke of magic increase the *size* of the separate mills.

Moveover, the economy of the trust form of organization is to be appraised, not by its efficiency as compared with individual plants alone, but by comparison with a combination of plants not possessing monopoly power. Clearly some of the saving that results from specialization can be secured by a combination, though it may well be that only a trust can realize this saving in full.

The economies of specialization are not open, however, to all trusts in the same degree, and to some not at all. Thus whenever a trust makes largely a single product with comparatively few grades, little, if any, economy through specialization is possible. In this respect the sugar and salt trusts, for example, stand in marked contrast to the steel and tobacco trusts.

(3) Specialization of ability. The trust, because it is such a huge organization, permits the fullest specialization of business ability. The president of the American Tobacco Company found the chief advantage of the tobacco trust in "the combination of talent," by which he referred no doubt to the union of the officials of the separate companies in a common enterprise and their distribution in that enterprise to the position for which they were best suited. That the trust combines most of the talent of the industry is obvious, yet it is not so clear that it possesses any marked advantage in the effective distribution of its talent over a combination or even a large individual concern. However, it unquestionably does offer a greater opportunity to those gifted individuals who have the requisite executive and organizing ability to manage a trust.

(4) Employment in each plant of the best devices, including patents. When a group of independent establishments are combined in a trust, the most effective labor-saving and other

devices that have been developed in any one plant may without restriction be employed in them all. This is an undoubted gain. Since the separate plants reflect and embody the ingenuity of officials forced to adopt improvements if they are to succeed in the competitive struggle, it may be assumed that some are more efficient in one regard and some in another. With the plants brought under a common management there takes place an interchange of ideas and the adoption in each plant of the most beneficial features of each. Of course, this is possible also to a combination, though not to the same degree. The question would remain whether once the trust was well established there would continue the same eagerness to eliminate wasteful methods and to introduce improved ones.

The same gain is open to the trust with respect to those devices that are covered by patents. Under competition one company might have a patent on one branch of the productive process, and other companies might have patents on other branches. Unless the patented device is available to everyone on a royalty basis, as is ordinarily not the case, no one company is able to make the most advantageous use of the results of invention. Through the common ownership of patents the trust effects a clear saving, though, to be sure, the saving is a temporary one, in view of the limited life of a patent. It does not follow, however, that this is an argument for the trust; it may merely prove the desirability of effecting certain modifications in our patent system. It would be entirely possible to permit the fullest use of all patents by anyone, reimbursing the inventor by means of royalties or by means of governmental purchase.[1] In this way the common use of patents would be made possible, and competition for the product of the inventor would be maintained.

Conceding that the trust effects a saving through a combination of patents, there still remains a very practical consideration

[1] The Chemical Foundation, whose stock is held by American manufacturers of chemicals and dyestuffs, leases all the German chemical patents that were taken over by the Alien Property Custodian to any manufacturer who makes application, and who pays the royalty charge.

bearing on the comparative efficiency of the trust as a permanent factor in our economic life. This is the question whether the trust is likely to promote invention.[1] Because of its financial strength, the trust, of course, can employ a staff of inventors, chemists, and other technical experts to invent new devices and to develop improved methods. Yet so can any large company or combination possessing adequate financial resources. Thus, Mr. Steward, of the International Harvester Company, testified that each of the companies that went into the trust had had a force of inventors and experimenters; and that Mr. Deering was "noted for expending large sums of money for experimentation."[2] Much evidence along this line might be presented, yet it is hardly necessary, since it is clear that this expenditure is one that depends on large-scale operations and financial strength rather than on combination.

Yet though trusts endeavor to promote invention and experimentation there is some reason to believe that they are less successful in this regard than their predecessors. In the first place, when monopoly exists the inventor has less inducement to exercise his inventive ability. His market is a more limited one, since in the main he must sell to the trust; and his rewards are therefore likely to be less. Under certain circumstances he may produce the patented article in competition with the trust, yet usually this is not feasible, since most inventions are simply improvements at some stage of a productive process already well covered by patents. Secondly, there is some tendency under trust control for experimentation to proceed along more narrow lines.[3]

[1] For a further discussion of this point see p. 535.

[2] Brief for the United States in International Harvester Company *v.* United States (no. 757), p. 130.

[3] A group of prominent manufacturers, who were instrumental in organizing the Shoe Manufacturers' Alliance, representing about 40 per cent of the shoe production of the country, declared in 1912 that whereas nearly every year from 1870–1900 had witnessed some marked advance in shoe machinery, with rich rewards for inventors, such new inventions as had been made during the period since 1900 (the trust was organized in 1899) were relatively unimportant. This check on the development of invention they attributed to the organization of a trust, which removed the stimulus of

Were the trust, through its corps of inventors, to discover some improved method of production that involved the scrapping of its old machinery or even its old plant it might well hesitate, were competition absent, to introduce the improvement, since the trust would have to bear the loss involved in abandoning the old machinery or plant. Under a competitive régime with patents open to all upon the payment of royalty an established concern would have to keep up with industrial progress, or give way to some other concern, possibly a newly established enterprise. But a trust, having a monopoly of its invention for seventeen years, is under no such compulsion. Mr. Knauth has recently called attention to the social loss that is involved in this wide destruction of capital under competitive conditions, and has implied that society would be justified in discouraging the adoption of a new invention, unless the resulting saving is sufficiently great to compensate for the destruction of existing capital that is rendered antiquated by the new process.[1] There is truth in this contention, yet the interests of society in the long run would appear to be best promoted by giving free opportunity to inventive genius, no matter whose ox is gored. As Mr. Knauth himself points out, one invention frequently leads to another; and there is thus an obvious danger in retarding the introduction of one improvement because of the social loss of capital, when the new invention may in turn lead to others that will more than compensate for all past obsolescence.

(5) Competition between plants. The trust by uniting a number of plants engaged in the manufacture of the same article or articles is in a position by means of a comparison of costs and other records to stiumlate a wholesome rivalry among plants and departments. If at any factory a given item of cost is abnormally high, the trust managers can require an explanation thereof, and unless it is due to some ineradicable cause can bring about an improvement in this regard. The result is a tendency toward a general leveling up of efficiency. Professor

competition. Report of the Senate Committee on Control of Corporations, 1913, pp. 2266–2267.

[1] Political Science Quarterly, 30, p. 580.

Jenks holds that the competition that arises in this way is more far-reaching than under a competitive régime, since the exact cost and efficiency at the separate plants are known, and the pressure to make a good showing is great.[1] The argument has weight, yet it is a question whether a salaried manager, even with a stake in the profits, would strive as earnestly to make a good showing as an independent business man for whom inefficiency means not only the failure to secure large profits, but the actual sustaining of losses. Be that as it may, the gain that accrues from competition among plants is open to the combination as well as the trust, though doubtless to a lesser extent. However, no gain on this score is possible, even to the trust, when the practice has been followed of specializing each plant on the production of a given shape or size. Obviously if each plant is devoted to the manufacture of a single machine or size to secure to the fullest extent the economies of large-scale production, no basis exists for a close comparative study of the separate plants. This point illustrates what many writers have apparently not seen, namely, that to enumerate a list of trust economies and to illustrate each by some one trust leaves the reader with the mistaken impression that each economy may be realized by all trusts. The fact is, as will be pointed out in discussing other economies, that the resort to one saving often precludes the employment of another; and that a number of economies may be availed of only by a comparatively few trusts.

(6) Utilization of by-products. Trusts can effect as complete a utilization of by-products as is feasible. Yet this saving results from production on a large scale rather than from combination. That this is the case is indicated in the fact that many writers fail to mention the utilization of by-products in enumerating the advantages of trusts. Those writers who do mention it commonly cite the meat-packing plants, and refer to the conspicuous absence of waste in these establishments. The fact is, however, that such combination as exists in this business is of the nature of a pool rather than of a trust. The leading companies have

[1] Jenks, Trusts and Industrial Combinations, Bulletin of the Department of Labor, vol. V, no. 29, p. 675.

undoubtedly largely eliminated competition, yet they have done so through agreement rather than through combination; and it is by virtue of the large scale of their individual operations rather than by virtue of their agreement that they realize these economies. Moreover, in some industries there are no by-products, and therefore there is no need of a trust to insure their effective utilization. Thus, in the manufacture of many steel and tobacco products there are no by-products; and in the refining of cane sugar there are only two of importance (molasses and sirup).[1]

(7) Insurance. Trusts can save in insurance, particularly fire insurance, because of the wide distribution of their plants. This possibility exists in some instances, yet not in all. Thus, the cash register trust with only one factory has no such distribution; and other concerns, the sugar trust, for example, have only a few plants, and therefore find it necessary to continue their insurance. Some combinations, such as the American Agricultural Chemical Company, have a wider distribution of plants, and thus of risks, than many trusts. It is quite obvious that the saving in insurance, when it exists, has not been of sufficient consequence to exert any considerable influence on the trust movement.

(8) Smaller fixed charges per unit of product. The trust with its large output has an advantage because its fixed charges are distributed over more units, and thus the expense per unit is less. This, however, is really an argument for large-scale production, and not for the trust. In every industry that has a national market, plants of a certain size secure full economic efficiency; and any expansion of the plant beyond this point, unless it takes the form of a complete duplication of the plant, is more likely to increase operating costs than to reduce them.[2]

[1] Report of the United States Tariff Commission on Costs of Production in the Sugar Industry, p. 23.

[2] This opinion is generally held by leading economists. See Taussig, Principles of Economics, I, p. 59; Ely, Monopolies and Trusts, p. 165; Bullock, Quarterly Journal of Economics, 15, p. 198; and Durand, The Trust Problem, p. 69.

This follows from the fact that a plant of a given size permits machinery to be employed in the most effective manner, and permits the most advantageous subdivision of labor; represents, in a word, the most effective combination of the productive factors, any variation from which increases rather than decreases costs. Failure to attain this effective combination of the productive factors means high costs and perhaps bankruptcy. Naturally, the size of the most economic plant unit varies greatly in different industries. Thus, the president of the large steel firm of Jones and Laughlin stated in 1901 that the minimum cost in manufacturing steel was not secured until an output of 2,000 to 2,500 tons per day was reached, but that a mill with this large an output could manufacture as cheaply as one that made 5,000 tons per day.[1] An independent refiner of cane sugar after considerable experimentation concluded that an output of 7,500 barrels a day was the most economic unit in this industry.[2] If the trust chooses the plant unit of maximum efficiency, it secures the economies of large-scale production; if it fails to do so, it does not secure these economies. Inefficiency in this regard, be it noted, may more than counterbalance all the savings that the trust can effect in other ways, namely, those economies that it realizes through the fact of being a trust. In other words, the reduction in fixed charges per unit of product above referred to is an economy of large-scale production and not of combination. If there be any industry in which the most efficient plant unit is one producing the total output, there will be in that industry a strong, probably irresistible, tendency toward monopoly;[3] yet the gains of monopoly will arise, not from combination, as with the trust, but from large-scale production. In this industry as in all others there should be no interference with the economic tendency toward large-scale production, yet public policy would doubtless demand that this industry, like all other natural

[1] Industrial Commission, XIII, p. 505. On the tin plate industry, see Dunbar, The Tin-Plate Industry, p. 102.

[2] Hearings on the American Sugar Refining Company, 1911–1912, pp. 1151–1152.

[3] The cash register industry may be one of this type. See p. 529.

monopolies, be brought either under the control or the ownership of the state.

III. *Economies in Selling*

The economies in selling may be discussed under the following headings: (1) advertising; (2) traveling salesmen; (3) export trade; (4) cross freights; (5) bad debts; (6) smaller stock of goods. It is in selling costs that the trust apparently finds the best opportunity for effecting economies that represent social gain.

(1) Advertising. The expenditure for advertising under conditions of competition is enormous. If this expenditure had the effect of stimulating the demand for commodities and thus of permitting large-scale production, it is possible that the expense of advertising might be compensated for by reduced production costs; and the cost and price of the article need not be increased on account of advertising expense. While this is sometimes the case, more commonly, no doubt, the effect of advertising is to increase the sales of one article at the expense of another. When this is the result, that is, when advertising does not increase purchases but merely turns them into different channels, the outlays for advertising must be regarded as economic waste, unless indeed the advertised article happens to be better than the one that would have been purchased had it not been for the advertising. The social costs of competition on the selling side are undoubtedly great; and their reduction is ardently to be desired.

Herein lies one of the principal advantages of the trust. The trust with the greater part of the market in its control need not expend such large sums to induce people to buy its product, since in large measure they must buy from it as the principal source of supply. Thus, the advertising expenditures of the tobacco trust declined as its monopoly control increased; and the advertising expenditures of the companies that succeeded to the trust upon its dissolution increased as compared with those of the trust. Illustrating the first point, the tobacco trust prior to 1900 controlled approximately 55 per cent of the output of

little cigars, and spent on advertising about 10 per cent of its net receipts (from little cigars) less tax; and between 1905 and 1908 it controlled approximately 85 per cent of the output, and spent only about 1 per cent of the net receipts less tax.[1] In part the large apparent saving resulted from the fact that the expenditures during the period when the trust was building up its monopoly control were abnormally large,—larger than they would be under normal competitive conditions. Thus, between 1898 and 1903 the trust was striving to obtain a monopoly of the manufacture of cigars, and in the latter year it actually expended on advertising 33.4 per cent of its net receipts less tax.[2] But having come to the conclusion that economic conditions did not favor monopoly in the manufacture of cigars, the trust gave up its competitive campaign, and by 1907 was spending on advertising only 4.7 per cent of its net receipts less tax.[3] Illustrating the second point, the advertising expenses of the tobacco trust in 1910 in all branches except cigars were $10,895,132, while those of the successor companies (the companies that succeeded to the business of the trust upon its dissolution) amounted in 1913 to $23,623,564, or more than double.[4] Based upon rates per thousand or per pound the advertising expenditures of the successor companies exceeded those of the trust by percentages varying from 14 per cent (Turkish cigarettes) to 155 per cent (plug cut smoking).[5]

These increases in cost seem to be properly laid at the door of dissolution; they represent some of the inevitable wastes of competition. The competitive system, of course, is by no means perfect; if it were none would seriously think of restraining its influence. And chief among its imperfections is the waste involved in inducing customers to buy the product of one concern rather than of another, even though the product of the latter be as good or actually better than that of the former.

Conceding that trusts may effect savings in advertising, it

[1] Report of the Commissioner of Corporations on the Tobacco Industry, part III, p. 5.

[2] Ibid.

[3] Ibid.

[4] Ibid., p. 18.

[5] Ibid.

should be realized that this saving is not always possible, and when it is possible the amount of the saving is often overestimated. Even under a competitive régime there were some articles that were not advertised to any considerable extent, since they were standard in character and in insistent demand. Others were marketed almost entirely through middlemen or a few large individual consumers. Still others were purchased as the result of chemical and other tests, and not as the result of advertising. Whenever advertising costs were negligible under competitive conditions, there was no opportunity for saving through the organization of a trust. For example, the steel trust hardly effected any notable economies as regards the advertising of steel rails; and neither did the sugar trust as regards the advertising of sugar.

Again, there are certain articles that were widely advertised in the days of competition, and that the trust still finds it necessary to advertise, though perhaps on a reduced scale. Thus, the tobacco trust, notwithstanding the fact that its control of the plug tobacco output increased from 56.3 per cent in 1899 to 84.9 per cent in 1910, was expending on advertising in the latter year 6.5 per cent of its net receipts less tax as against only 4.8 per cent in 1899.[1] These increased expenditures were necessary because otherwise the public might have consigned chewing tobacco to everlasting oblivion. Other trusts that have found it necessary to advertise are the photographic camera, gunpowder, glucose, starch, whisky, silver-ware, and chewing gum trusts, to cite but a few. The managers of these concerns have learned that their sales fall off with marked rapidity, once they fail to remind the public of its needs; and the same holds true in considerable measure of all trusts except those producing the staple, essential articles. This would still be true, even if all industries were under the control of 100 per cent monopolies; for a great many trusts, e. g., the camera, watch, tobacco, silver-ware, wall paper, aluminum, and bicycle trusts, would still be in competition with each other for the trade of the buyer, and each, therefore, would

[1] Report of the Commissioner of Corporations on the Tobacco Industry, part III, p. 5.

have to advertise to maintain its position. The trust, therefore, has found that it may easily lose more through reduced sales than it gains through diminishing advertising expense.

Another group of trusts embraces those that spend even more on selling than do their competitors. Thus, the selling expenses of the International Harvester Company per machine were considerably greater than those of the independent concerns.[1] These expenses were only in part advertising, to be sure, yet no doubt its advertising expenses were greater than those of its competitors. This relatively high expense resulted apparently from a policy of increasing the volume of sales by the maintenance of an elaborate selling organization rather than by the reduction of prices. Undoubtedly this was the best policy for the company, yet it is important to note that the so-called competitive wastes of selling were not eliminated by the establishment of a trust.

(2) Traveling salesmen. Since much of the energy of traveling salesmen was directed to inducing the buyer to purchase the goods of one manufacturer rather than another it was only to be expected that with the establishment of a trust much of this personal solicitation could be eliminated. The whisky trust, for example, dispensed with 300 traveling salesmen, and effected a saving of $1,000,000 a year in the Kentucky branch alone.[2] The wire trust (the American Steel and Wire Company) dispensed with about 200 traveling salesmen. In other cases it was found possible to replace high grade salesmen, adepts in persuasion, with reliable but less expensive individuals. The Royal Baking Powder Company replaced salesmen receiving $4,000 to $5,000 a year with men paid less than $1,000 a year.[3] That notable savings were effected was admitted in substance by Mr. Dowe, the president of the Commercial Travelers' National League. He estimated in testimony before the Industrial Commission that more than 35,000 salesmen had lost their

[1] Report of the Commissioner of Corporations on the International Harvester Company, p. 262.

[2] Industrial Commission, I, pp. 829–830.

[3] Ibid., p. 32 (Testimony).

positions as the result of the organization of trusts, and that about 25,000 others had suffered a reduction in salary.[1]

That trusts may realize some economies in this fashion is obvious. As with advertising expenditures, however, the possibility does not always exist; and when it does exist, its importance may be exaggerated. In some cases the organization of a trust did not lead to any economy in this direction. The president of the wall paper trust testified that it sent out more traveling salesmen than the predecessor companies;[2] and the president of the silver-ware trust, that it sent out as many, and probably more.[3] Even after the sugar trust was formed a leading competitor (Arbuckle Brothers) employed no traveling salesmen.[4] The tin plate trust achieved no important saving in this way, since the thirty-nine companies that preceded the trust did not have in the aggregate more than ten traveling salesmen.[5]

Even when the possibility of a saving is present its importance must not be exaggerated. The wire trust did succeed in reducing its force of salesmen, yet it had no notion that it could successfully compete with the Carnegie Steel Company, if the latter saw fit to engage in the manufacture of wire goods. Apparently the saving in salesmen was not a controlling factor. The whisky trust announced large savings, yet as a trust was distinctly unsuccessful. There is reason to believe that the trust organizers and officials in the first flush of their enthusiasm overestimated the possible savings. This is substantially conceded by Mr. Flint, the organizer of a number of trusts. Testifying before the Industrial Commission he said that in many cases trusts had undertaken to secure too great economies, and had thereby

[1] Industrial Commission, I, p. 27 (Testimony). No doubt there is included in these totals those salesmen who had been employed by combinations popularly referred to as trusts, yet not possessing monopoly power. Mr. Dowe therefore exaggerated the savings resulting from the organization of trusts.

[2] Ibid., XIII, p. 292.

[3] Ibid., I, p. 1059.

[4] Ibid., I, p. 147 (Testimony).

[5] Ibid., I, p. 877.

diminished the efficiency of the selling department and reduced the sales in proportion.[1] The rubber goods trust, which he had organized, avoided this difficulty. The policy of its management was to sustain the individuality and independence of each concern, even at greater expense, since experience had shown, he maintained, that it was not advantageous to attempt to secure the last economy. It is probable also that the trust managers failed to allow sufficiently for the contribution of their salesmen. As Professor Dewing well puts it: "Few things count more in salesmanship than the personal magnetism of an able salesman basing his appeal on long established trade connections. The directors of the consolidation sought in the interest of organization and economy to replace high salaried salesmen by low paid order clerks. Many of these salesmen had been the proprietors of the old businesses, men who held their customers by family association. . . . 'Among the oldest houses doing business with us' was a bond which the force of circumstances broke with difficulty. Instead of profiting through this bond the new order of scientific salesmanship interposed the deadening influence of organization between buyer and seller. Customers found that they were no longer dealing with the son of their old friend, but with some cog in the machine designated as A B C. . . . As a result they often turned elsewhere." [2]

(3) Export trade. Much has been made of the advantage of the trust in developing the export trade. The president of the American Steel Hoop Company (the hoop trust) maintained that his organization was able to develop foreign business in a way not open to smaller concerns; that the company's large capital and business made it possible for it to spend large sums in pioneering, and to employ agents all over the world. The same claim was made for the United States Steel Corporation, organized two years later as a combination of a number of steel combinations and trusts, including the American Steel Hoop Company. Other trusts which have emphasized the importance of capturing foreign trade, and the necessity of a trust for that

[1] Industrial Commission, XIII, p. 35.

[2] Corporate Promotions and Reorganizations, p. 561.

purpose, are the harvester, tobacco, and oil trusts. In the organization of some trusts, however, no pretense was made that the expansion of the export trade had anything to do with the formation of the trust. The sale of tin plate in the world's markets was regarded as a possibility only in the "long future";[1] and an export trade in rubber shoes was not anticipated, since the raw material had to be imported, and since the manufacture was carried on largely by hand labor paid the high American wage scale.[2]

The export trade may be developed in two ways: (1) By the normal and proper process of offering a good article at a reasonable price under conditions, such as provision of credit facilities, that make it desirable and possible for the foreign consumer to purchase. To build up trade in this way may necessitate a study of the needs of foreign buyers, and perhaps an intensive campaign to convince them of the advantages of the American product. (2) By resort to the practice of dumping, that is, the sale of the exported article at a lower price than is charged at home.

So far as the latter method is concerned, the trust undoubtedly has an advantage over concerns in industries that are characterized by competitive conditions, assuming, of course, that a high tariff barrier prevents the dumped article from being returned to this country. The trust can afford to sell a part of its output abroad at a comparatively low price, since the gain that results from maintaining the domestic price largely accrues to it; whereas an individual concern can not do this, since it would be mainly its competitors that would profit by the maintenance of a high price in the home country. The justification ordinarily offered by the trust for favoring the foreign consumer as compared with the domestic consumer is that the sale of a part of the product abroad, even at lower prices than at home, is profitable to the trust, since it permits operation at capacity and thus at lower cost; and is advantageous to the public, since it gives steadier employment to labor and reduces the fixed

[1] President Reid in Industrial Commission, I, p. 882.

[2] Industrial Commission, XIII, pp. 80–81.

expenses per unit of product. In analyzing this point and its relation to trust economy it may be inquired whether the dumping practiced by the trust is to be sporadic or regular. If the former, it is clear that the trust would not succeed in building up an export trade; for obviously it is not possible to develop the export market by sales to foreign customers only at those times when the home market will not absorb the whole output at satisfactory prices. Foreign consumers, if treated in this fashion, will turn elsewhere for their major purchases.[1] If, on the other hand, the dumping is to be permanent, what becomes of the argument that operation at capacity and steadier employment to labor is possible? Clearly there is no special virtue in foreign sales persistently carried on, except the general advantage that comes from having a wider market, that enables a company engaged in foreign trade to avoid those recurrent periods when the producing capacity exceeds the demands of the market. Suppose the foreign trade plus the domestic trade equals the productive capacity of the country in any particular line. If the demand for the product increases, as it normally does in a growing country like our own, the productive capacity in time will be increased to take care of the demand; when the demand declines, as it does at irregular intervals for nearly every commodity, an excess capacity will temporarily appear. The fact that the trust has established a permanent foreign business through a persistent policy of dumping will not prevent the occasional emergence of surplus producing

[1] This would be less true of such exports as steel products than it would be of cigarettes, or binders and binders' parts. Nevertheless we have the testimony of Mr. Farrell, the president of the Steel Corporation, that it is true of steel products also. Testifying in the government suit he declared that it was impossible to develop a foreign business unless it was done continuously, because buyers would refuse to patronize concerns that were not in a position to serve as a continuous source of supply. Brief for the United States in United States *v.* United States Steel Corporation (no. 481), vol. II, p. 614. Having long been in charge of the exports of the Steel Corporation, Mr. Farrell was in a position to know whereof he spoke. For further evidence see Report of the Federal Trade Commission on Cooperation in American Export Trade, I, pp. 374–375.

capacity. The trust may, to be sure, temporarily secure relief by sporadic dumping designed to attract a new set of foreign buyers, yet this, as has just been pointed out, does not conduce to the permanent development of our foreign trade.

It may be inquired next what advantages the trust has with regard to what we have called the normal and proper method of developing export trade. Perhaps the principal condition prerequisite to the capturing of foreign trade is the possession of abundant financial resources.[1] In developing the foreign market it may be necessary to create an extensive organization and to make large outlays in the form of advertising, sales agencies, and so forth; and to retain the foreign market an extension of credits will probably be necessary. Only a concern with large capital can expect to succeed in such an undertaking. However, this, as the Industrial Commission stated, "does not necessarily imply monopoly."[2] Much has been said about foreign trade in connection with the International Harvester Company. Yet the McCormick and Deering harvester companies prior to the organization of the trust were expanding the foreign trade very rapidly.[3]

[1] We shall not discuss such essential conditions as the building up of a reputation for honesty and quality, and the manufacture of goods to meet the particular wants of foreign peoples. These do not appear to have any special relation to the trust problem. For the same reason we may omit discussion of such matters as the provision of banking facilities abroad, the maintenance of an American merchant marine, and American investments in foreign securities.

[2] Industrial Commission, I, p. 23 (Digest).

[3] Brief for the United States in International Harvester Company *v.* United States (no. 757), pp. 124–125. The officials of the International Harvester Company pointed out that the foreign trade in harvesters up to 1902 was handled through foreign jobbers, who generally bought for cash and sold to the owners of large estates on the same terms; and they claimed that this method of selling machines could not be successfully employed with small farmers, especially in the newly developed countries that needed machines the most. To reach this group it was necessary to establish branch houses with large stocks, and to sell direct to the farmer on credit; and this involved a more elaborate selling organization and greater resources than did the jobbing system of distribution, in fact, greater resources than any American company possessed. Brief for the International Harvester Company in International Harvester Company *v.* United States (no. 56), pp. 54–56.

Whether the trust increased this trade more rapidly than separate companies would have done a federal court found to be a "mere matter of speculation." [1] It is quite probable that it did, yet it is significant that in 1913, under some pressure, to be sure, from the government, the foreign business (with the new lines) was turned over to a newly organized corporation (the International Harvester Corporation) which certainly was not a trust. To give another illustration, the Plymouth Cordage Company, an independent cordage concern, sold its products "nearly all over the world." [2] Trusts in general, it may be conceded, are more likely to have the requisite capital to promote export dealings, yet even individual concerns may be well fortified in this regard. Moreover, under the Webb-Pomerene Act they may now combine to this end without violating the anti-trust laws.[3]

Another prerequisite is the possession of an output sufficiently large to justify a foreign organization service. Practically every trust, of course, could qualify on this score, yet so could many large individual concerns and most important combinations. If not, it is now legal under the Webb Act to coöperate for this purpose.

In competing for foreign business there is an advantage in possessing strategically located plants. The Standard Oil Company with a refinery at Bayonne, New Jersey, the American Tobacco Company with a factory at New York City, and the International Harvester Company with a plant at Auburn, New York, were well situated in this respect. However, there is obviously nothing to prevent a mere combination from distributing its plants with an eye to the export trade, and nothing to prevent an individual enterprise locating its plant in such manner that it can effectively engage in foreign commerce. The Bethlehem Steel Corporation, for example, is better off in this respect than the Steel Corporation, since its rail haul to the Atlantic seaboard is less.

There is a further advantage in some instances in manufactur-

[1] 214 Fed. Rep. 993.

[2] Industrial Commission, XIII, p. 140.

[3] See ch. 16.

ing a variety of products. A sugar or a starch trust would have little, if any, advantage in this regard over an individual concern; but a steel, harvester, or cash register trust manufacturing a full line might have a considerable advantage over a concern that manufactured, let us say, only wire products. The president of the Steel Corporation declared that it would have been impossible for the constituent companies of the Corporation, had they remained distinct, to have developed the foreign trade as the Corporation has done; that a concern to do a successful foreign business must be able to offer all lines of products, since one product sells another and since the buyer usually wishes to secure his whole supply from one source.[1] There is much force in this contention, though the enactment of the Webb law should do much toward placing less far-reaching concerns in a more favorable position in this regard.

The limitations on the ability of trusts to develop exports should be borne in mind. The product of some industries is not suitable for export, or at least is not exported. The exports of anthracite coal and salt, and no doubt, of tin cans, are so small that there is not a particle of justification for a trust in these branches on the score of their ability to build up the export trade more effectively. In other branches of industry, though there is nothing in the nature of the product to prevent, even a trust fails to develop the export trade. The sugar trust illustrates this case; its exports up to the period of the war were an insignificant proportion of its total sales. The exports of tobacco products other than cigarettes are quite small. Again, in a few instances the export business is deliberately sacrificed as a means of keeping foreign manufacturers out of the home market. The powder trust, for example, entered into an international agreement in 1897, to last for ten years, whereby it agreed in return for a monopoly of certain territory to sell *no* high explosives in Europe, Africa, or Asia.[2]

[1] Brief for the Steel Corporation in United States *v.* the United States Steel Corporation (no. 481), p. 116.

[2] Petitioner's record in United States *v.* E. I. du Pont de Nemours and Company (no. 280), Exhibits, vol. II, pp. 1123–1132.

Concluding with regard to this economy, it appears that in some branches of industry the trusts when first established were better situated to develop the export trade than their predecessors, but that with the passage of the Webb-Pomerene Act this advantage has been much reduced, and may largely disappear.

(4) Cross freights. The trust, owning a number of plants can supply the market, it is said, from the nearest plant, thus saving cross freights. The president of the wire trust estimated the cross freights at $500,000 a year, and claimed a saving in this way through the establishment of the trust.[1] In the salt industry a large percentage of the price is made up of the freight rate, and the trust, so it is averred, made an enormous saving.[2] When the product to be shipped is bulky, the trust may achieve an economy in this regard, though there are a number of considerations that reduce the importance of cross freights as a trust economy. First, a combination not possessing monopoly power, yet owning a number of well-distributed plants, can also reduce cross freights; the gain realized by the trust is only the additional saving that is not open to the combination.[3] Second, if the monopolized article has large bulk in proportion to its value, that is, if the freight rate is an important element in determining the price, the plants are likely to be widely dispersed prior to the organization of the trust; and thus the possible saving is less than might at first thought appear. The manufacture of tin cans supplies an excellent illustration. Third, if the monopolized article has high value in proportion to its bulk, that is, if the freight rate is relatively unimportant, the trust can save little. So far as cross freights are concerned, there is little to be gained through the organization of trusts in the watch, whisky, tobacco, thread, chewing gum, and silver-ware industries. In the silver-ware industry not only were transportation charges relatively

[1] Industrial Commission, I, p. 1030.

[2] Montague, Trusts of To-Day, pp. 65–66. See also Industrial Commission, XIII, p. 253.

[3] The National Steel Company, a large combination, but not a trust, claimed economies through the elimination of cross freights. Industrial Commission, I, p. 947.

unimportant, but the plants of the trust were so concentrated in a particular locality that one plant could supply the market as well as another. Fourth, there are some industries in which the economies of large-scale production are apparently so great that it is advantageous to concentrate the entire output in one plant. For example, the National Cash Register Company makes all its cash registers at Dayton, Ohio. Obviously it can not save anything by the elimination of cross freights. Fifth, in some industries the location of the plants is determined by natural factors that permit of no saving in cross freights. The best illustration perhaps is the anthracite coal industry, an industry characterized by a very high degree of localization based on natural conditions. Finally, a saving in cross freights is possible to only a limited degree, if at all, in those cases in which a trust has secured the economies that result from specialization. If the steel hoop trust chooses to manufacture all of its hoops of a certain size in one factory to secure the economies of large-scale production, it must supply the entire market from that particular factory, and can therefore save nothing in cross freights. Again, if the tobacco trust, prior to its dissolution, found it advantageous to manufacture four-fifths of its cigarettes in three factories,[1] none of which was 200 miles west of the Atlantic Ocean, it must be because it chose to realize the economy of large-scale production rather than of lower freight rates. This is the situation, it should be noted, whenever a concern concentrates a particular brand, whether it be tobacco, starch, or what not, in one factory.

(5) Bad debts. The trust, not being subject to the pressure of competition to the same degree, can avoid undue extensions of credits to purchasers, and thus need not sustain such large losses in the way of bad debts. The stock illustration is the American Steel and Wire Company, which reduced its percentage of loss from bad debts from one-half of one per cent to one-twenty-fifth of one per cent. Undoubtedly many trusts have been able to save in this way, yet clearly the saving is slight. Moreover, some trusts, notably the harvester trust, find it necessary to

[1] Report of the Commissioner of Corporations on the Tobacco Industry, part I, p. 340.

make wide extensions of credit even at the risk of some loss. It is safe to say that no trust which would not have been formed otherwise would be formed in order to reduce the loss from bad debts.

(6) Smaller stock of goods. The trust by virtue of the fact that it covers the country and handles such a large percentage of the total output does not need to carry such large stocks; its managers are in a better position to gauge the requirements of the market. In so far, moreover, as the trust promotes the standardization of parts, it reduces the quantity of stocks required. The reduction in stocks naturally means a saving in interest, insurance, storage, and shop wear charges.

Disadvantages of The Trust Form of Organization

Having enumerated the economies of the trust form of organization, and examined the extent to which they are of significance, we may turn to a consideration of certain factors that act as an offset to these economies and tend, in so far as they have weight, to make the trust an actually less efficient business unit, particularly when viewed over a long period of time. These countervailing factors are: (1) the scarcity of, or failure to secure, the high order of administrative ability required in the management of a trust; (2) the difficulty of enlisting the best services of the operating officials; (3) the tendency of monopoly toward stagnation; (4) the additional financial outlays to which trusts are subjected; and (5) the burden of a highly centralized administrative machinery.

(1) The first consideration that calls into question the superior efficiency of the trust as a business unit is the scarcity of that high grade of executive and administrative ability that is required to manage a business of the dimensions and ramifications of the trust.[1] Few of the men who can manage a single mill with a high degree of efficiency can manage a combination of mills successfully; and very few of those who can manage a combination successfully can do the same for such an all-embracing

[1] For some opinions of business men on this point, see Industrial Commission, XIII, pp. 84, 133.

combination as the trust. This point of view has been well expressed by President Hadley. "Just as in an army there are many who can fill the position of captain, few who can fill that of colonel, and almost none who are competent to be generals in command—so in industrial enterprise there are many men who can manage a thousand dollars, few who can manage a million, and next to none who can manage fifty million." [1] The mere work of centralized administration, he said, puts a tax upon the brains of men who are accustomed to a smaller range of duties, which very few find themselves able to bear. There can be no doubt that through organization, aided by modern methods of prompt communication, the effective directing power of the administrator has been much increased. Nevertheless even the best organization requires direction and supervision. The success or failure of an enterprise, in fact, is usually determined by one man; and there is a definite limit to what one man can do. The increase in the size of the business, particularly one extending over a wide area, increases greatly the number and variety of the problems that an executive has to solve, and makes it more difficult for him to exercise a sound judgment upon them. Moreover, the consequences of errors in judgment are particularly harmful, since they affect a whole industry, instead of merely a single plant.

If it be granted that there are executives able to administer a trust effectively in competition with a less ambitious undertaking, the question would remain whether they could be induced to serve as the salaried heads of the trust. "Captains of industry" have been known to refuse to accept positions at princely salaries, because of their unwillingness to be held in leading strings. The story is told of a prominent business man who indignantly rejected an offer of $100,000 a year, on the ground that he was expected to serve as office boy. Such individuals prefer to be their own masters; and if, as seems probable, the supply of capital seeking investment is increasing more rapidly than the superior grade of administrative ability required to manage a trust, they will be in a fair way to realize

[1] Scribner's, 26, p. 607.

their wishes, and thus the trust may suffer from inferior management. The same applies, of course, to that much larger number of capable business men who have the choice of holding responsible positions as salaried trust officials of one kind or another, or of being heads of individual enterprises. On the other hand, it may be said with reason that the trust could readily enlist in its service the most capable administrators by granting them the fullness of authority that they crave. The administration of the affairs of a trust is a task of great magnitude; and it may perhaps be presumed that the owners or directors of the trust, rather than rely upon inferior leadership, would give to the executive head as free a rein as was necessary to attract the best talent.

Granting, then, that the requisite administrative ability exists and that it *may* be enlisted, it does not follow that it *will* be enlisted. There is a possibility that the administration of the trust properties will be turned over to "friends rather than experts"; that the relatives of large stockholders or other financial interests will be taken care of to the detriment of the business. There is the same possibility, of course, in individual enterprises; in fact, the smaller the business the greater is the danger that personal favoritism will dictate the appointments to the higher positions. Nevertheless in smaller businesses the necessity for an unusual grade of talent is less pressing, and there would appear, moreover, to be more ground for expecting the son of a moderately capable business man to equal his father in ability than there would be to expect the same result in the case of a business man of unusual capacity. Genius, as has been well said, rarely breeds genius.

Granting all the foregoing points, the future alone could determine whether there will be a continuing supply of administrative leaders to serve as trust managers. It must be remembered that the heads of the trusts when first organized were men bred in the competitive struggle. Such degree of success as the trusts have achieved to date may result from the fact that they have been able to command the high order of talent that is trained in the rigorous competitive school. Were industry to be

free from the competitive pressure, it is conceivable that business undertakings would show a tendency to a reduced scale, because of the difficulty of securing the requisite executive leadership. As one writer has put it, "the development of a high order of undertaking genius in the few seems . . . to depend upon a wide range of undertaking experience in the many." If this be so, the removal of the educational ladder up which developing geniuses may climb might have serious social consequences. That no such results are to be anticipated in the immediate future results from the fact that the great mass of industry is still more or less competitive. This holds true even of certain branches that were once controlled by trusts; for in a number of industries, whether because of the unimportance of the economies of the trust form or because of the failure to secure the best leadership, the endeavor to maintain a monopolistic control has been a failure.

(2) Even if the trust can overcome the difficulties just described it is doubtful, it is said, whether it can enlist the best services of its leading officials. A salaried employee, say a manager or a superintendent, is hardly likely, it is claimed, to give such close personal attention to a plant in which he has no large financial interest as is an individual who owns the plant. The weakness of the trust on this score was conceded by Mr. Flint, the promoter of a number of trusts. He said, "One of the fundamental difficulties of the management of these corporations lies in the fact that the managers have a smaller percentage of interest in the operations that they are conducting under the plan of an industrial combination than they had when it was an individual property or when they had a large interest in a small corporation. That is fundamental. There is no way in which that condition can be changed." [1]

The most effective way in which the trust can enlist the interest of its salaried officials, as Mr. Flint pointed out, appears to be the introduction of comparative cost systems and the grant to the officials of a financial interest in the business. The adoption

[1] Industrial Commission, XIII, p. 85. For further testimony of business men, see ibid., I, p. 899, and XIII, p. 158.

of comparative cost systems may be expected to bring good results, either by appealing to the spirit of emulation, the desire to make a better showing than one's fellows; or by appealing to the spirit of fear, the dread of losing one's position. The grant of a financial interest in the business, perhaps through a salary based on output or cost, may also be expected to stimulate the interest and efforts of the salaried officials. Yet it is not always feasible to pay salaries based upon output, costs, or profits, as the case may be; and even when it is feasible it is doubtful whether the spur is fully adequate. So long as the salaried official has merely a stake in the profits, and does not have to bear the losses, if they materialize, he has not the double incentive that the owner of a business has. The salaried official, to be sure, may also own stock in the enterprise, and thus have an additional reason for putting forth his best efforts. In this event the contrast between a trust and an independent enterprise is not so striking, although the relationship between the efforts of a high official in a trust and his profits is not likely to be as close as the relationship between the efforts of the head of an independent business and his profits.

Concerns with a single plant, and to a lesser degree moderate-sized combinations, realize a further gain in that they can locate their executive force in close contact with the plant or plants; whereas trusts (and large combinations) must usually have their executive (and sales offices) separated from the manufacturing properties.[1] The farther removed the directing staff is from the operating branch, the more difficult does it become to check up on the work of the various plant managers. As one manufacturer put it, "there comes a point where the man in the twentieth story of an office building cannot make up, no matter how brilliant he may be, for the waste and shiftlessness of a variety of superintendents in many mills hundreds of miles away in all directions."[2]

(3) The trust, being a monopoly, is less likely, we are told, to

[1] When the plants of the trusts are concentrated in one town or region, no disadvantage is encountered on this score.

[2] See Dewing, Corporate Promotions and Reorganizations, p. 559.

apply new inventions or to adopt improvements that necessitate the scrapping of expensive plant and equipment.[1] As Professor Clark puts it, "a monopoly makes no proper use of that invaluable agent of progress, the junk heap." [2] During the period that preceded the trust movement American manufacturers were notable for their willingness to discard even good machinery and equipment in order to install improved facilities that promised to reduce the costs of production. It was this policy that made the Carnegie steel properties the most efficient in the country—so efficient that Mr. Carnegie could snap his fingers at the various steel trusts, notwithstanding their reputed economies. His view as to the strong position of his company he expressed in a letter to his associates, dated July 11, 1900. "We need," he said, "to manufacture hoops, cotton ties, steel wire, nails, tubes, perhaps other things later as we go on. Whenever we do so we have the big trusts at our mercy." [3] With the development of an established monopoly, however, a slackening in the march of improvement may perhaps be expected. Whereas competition provides a stimulus to the introduction of improved methods, the tendency of monopoly is toward stagnation. To be protected against competition, said John Stuart Mill, is to be protected in mental dullness;[4] and certainly there is much evidence to support this view. It is significant that leading railroad executives opposed the proposition to establish regional railroad monopolies, their contention being that it was essential that competition in service be maintained. The chairman of the Westinghouse Air Brake Company opposed it on the ground that it would retard invention. In a statement prepared for the Senate Committee on Interstate Commerce he said, "As a rule, railway managers were not over-enthusiastic about testing untried devices, and it became necessary to find the right man and auspicious conditions, in order that the desired development and

[1] See also p. 511.

[2] Clark and Clark, The Control of Trusts, p. 14.

[3] Brief for the United States in United States *v.* United States Steel Corporation (no. 481), vol. II, p. 473.

[4] Principles of Political Economy (7th edition), Book IV, chapter VII, § 57.

demonstration might be made. This process was greatly facilitated by the *number* of railways to which appeals could be made."[1] If it be urged that trusts have continued to make improvements, even of a far-reaching character, it may be pointed out that, except when they have been protected by patents or control of natural resources, they have experienced unexpected difficulty in maintaining their position, so persistent is the force of competition. Moreover, they have had to justify their existence before an aroused and hostile public opinion. It may be, therefore, that they have not as yet fully exhibited their natural tendencies. However, once monopoly became secure, its usual consequences might be expected to appear.[2] This, indeed, would doubtless be the outcome even though the trust were blessed with capable executives; for the financiers and capitalists that owned the properties would oppose the introduction of improved machines unless the resulting saving were sufficiently great to compensate for the loss occasioned by the scrapping of the old machines. An individual enterprise, to be sure, must sustain this same loss, yet it is able to reimburse itself through the increased business that its lower cost of production enables it to secure. It may be conceded, as stated elsewhere,[3] that the introduction of a particular invention or improvement may occasion a social loss, yet the possibility of an occasional loss in this way does not justify the adoption of measures designed to interfere with the progress of invention or the adoption of improvements.

(4) The trust is subject to some financial outlays that individual enterprises or combinations either do not have at all or have in lesser volume. First, the trust, owning a number of plants, often widely scattered, all of which are managed by salaried employees, must maintain an elaborate and expensive system of control and supervision. It must make unusually

[1] Hearings on Extension of Tenure of Government Control of Railroads, 65th Cong., 3rd Sess., vol. I, p. 1442.

[2] President Wilson, in fact, maintains that they have already appeared. See New Freedom, pp. 265–70.

[3] See p. 513.

heavy outlays in the way of bookkeeping, accounting, and auditing, and all the paraphernalia of administration designed to stimulate energy and economy on the part of its employees. Through these expenses the problem of administration may be solved, yet without them effective administration is impossible. The combination, and even the individual enterprise, is not free from these expenses, to be sure, yet their amount increases with combination, and is the greater the more far-reaching the combination.

Second, some trusts, though not all, are burdened with a number of antiquated, inefficient, and badly located plants that were bought to stave off competition, actual or potential. In so far as these properties were paid for in stock the cost of production is not increased; the effect is merely to reduce the rate of profit on the company's stock. In so far as they were purchased for cash or for issues of bonds they constitute a permanent drain on the revenues of the trust. Moreover, a number of other payments than those involved in the purchase of plants were often incurred, including the rent of factories to prevent them from operating, and the payment of salaries to former owners to keep them from building a new plant with which to compete with the trust. Such outlays deserve mention, though their importance must not be exaggerated.

Third, a considerable number of trusts have been enabled to maintain their monopoly only through the continual purchase of their most effective competitors. Trusts that have been notable in this regard are the sugar, tobacco, gunpowder, glucose, and starch trusts, and to a lesser degree the steel trust. Sometimes a high price has been paid to induce the independent concern to sell; at other times a severe competitive campaign has put the competitor in such a frame of mind that he has been willing to sell for a moderate or even low price. In either event the trust to maintain its monopolistic position has been put to additional expense.

(5) All large businesses, and therefore the trust in particular, are likely to suffer from the burden of centralized administrative machinery. The trust ordinarily possesses a number of plants

scattered throughout the country, and does a nation-wide business. Obviously an enterprise of such magnitude and dispersion can not receive the personal and close supervision of the executive. It is therefore necessary to establish a group of departments and subdepartments, and to institute an elaborate system of records and reports for the purpose of checking up the work of the separate plants and departments. From the point of view of the trust there is grave danger lest this "system" prove cumbersome and burdensome; lest it degenerate into bureaucracy and routine, into what in government departments is slightingly referred to as "red tape." An aversion to change is a well-known characteristic of all large administrations; and this is likely to be particularly true of a trust, the very economies of which are in the main those of systematization and standardization. On the other hand, there is the ever present possibility that the necessity of referring proposals for improvements and changes to the "higher ups" may deaden the enthusiasm and initiative of the subordinate officials. Thus there may arise, as Professor Bullock has well said, "an irrepressible conflict between that central responsibility necessary for intelligent, unified management and that individual freedom and energy requisite for the healthful life of the separate members." What is gained at the center in the way of control and guidance may thus be lost through reduced efficiency and energy at the circumference. These inherent disadvantages of large-scale operations apply, of course, also to individual enterprises and to combinations, yet the trust is particularly subject to them because of its size, the distribution of its business over a wide area, and most of all because the tighter the monopoly the less it feels the competitive spur.

The doubt that has been expressed as to the superior efficiency of the trust form of organization is increased upon an examination of the record of trusts. In view of the fact that most of the modern trusts were organized at least twenty years ago, sufficient time has elapsed to gain some insight into what is to be the verdict of history upon their future. During this period a large number of trusts have done so poorly that they must be regarded

as failures. Among these trusts are the following (in alphabetical order): asphalt, bicycle, cordage, cotton duck, cotton yarn, glucose, linseed oil, malt, news print paper,[1] paper bag, salt, shears and scissors, silver-ware, sole leather, starch, upper leather, wall paper,[2] whisky, and writing paper. The list is not complete, yet it is sufficiently long to show that the economies of the trust form of organization have often proved illusory, or, if not illusory, they have not been sufficiently important to offset the disadvantages peculiar to that form or organization. There are other trusts that may have been financially successful, yet have not succeeded in retaining a monopolistic grasp on the industry. The sugar and tin can trusts will serve as examples. The steel trust has shown a declining percentage of the country's output, yet on the whole seems to have the situation well in hand through a policy of coöperation with its more rapidly growing semi-competitors.

Does the fact that a number of trusts have not been failures, nay quite successful, prove the economies of the trust form of organization? It would not appear so. In an examination of a considerable number of individual trusts we have yet to find one the success of which is not explicable upon other grounds. Some trusts, notably the shoe machinery, the camera (and at one time the aluminum, gunpowder, and sulphur trusts) are founded on a grant of monopoly by the national government. Others, e. g., the aluminum, borax, diamond (an international trust), and chewing gum trusts, are (or have been) fundamentally based on the control of a natural resource. The steel trust might once have been placed in this group, but technical improvements that have permitted the economical utilization of lower grade ores than those that had been substantially monopolized by the

[1] The International Paper Company no longer has even the largest mill in the country, the largest mill being owned by the Great Northern Paper Company. Pulp and Paper Investigation Hearings, House Doc. no. 1502, 60th Cong., 2nd sess., 1908–1909, p. 1072.

[2] The head of this trust said: "It has . . . been demonstrated that the manufacture of wall paper involves elements of so peculiar a nature that it cannot be as successfully conducted through the medium of a combination as it can through independent and isolated plants." Chron., 71, p. 33 (1900).

Steel Corporation have taken away much of the advantage that the Corporation formerly enjoyed in this regard. The success of the working agreement in the anthracite coal industry is also based on the concentrated ownership of a limited natural resource. Other trusts have been the recipients of transportation favors, notably the oil trust and the sugar trust.[1] Still others, having once secured a monopolistic position by the act of combination, have maintained this position: (1) by the resort to unfair competitive tactics (e. g., the oil, gunpowder, tobacco, cash register, and sugar trusts);[2] or (2) by the purchase of the leading competitors (e. g., the tobacco, sugar, gunpowder, and in lesser degree the steel trusts); or (3) by virtue of the fact that the most efficient *concerns* were a part of the trust (e. g., the harvester, steel, and tobacco trusts). The harvester trust, the Bureau of Corporations found, had a lower cost of production than its competitors, yet this advantage appears to have resulted mainly from the fact that it included the McCormick and Deering concerns, easily the two largest manufacturers of harvesters in the country prior to the organization of the trust. No satisfactory evidence has been adduced to show that the cost of manufacturing harvesters at the plants of these two companies has been reduced as the result of the organization of the trust; in fact, it is probable that manufacturing (not selling) costs at the McCormick plant, at least, have been increased, for the output of binders and mowers at this plant since the formation of the trust has never equalled, and is now much less than, the maximum output in the period preceding the organization of the trust.[3] Again, a large part of such advantage, if any, as the steel trust now enjoys unquestionably results from the inclusion of the Carnegie works,—admittedly the most efficient steel plant in the country at the time of its acquisition. The Corn Products Refining Company owes much of its success of recent date to the fact that it took in the New York

[1] The steel trust has not enjoyed railroad rebates, yet it has occupied a strategic position through its ownership of iron ore railroads.

[2] For details see Stevens, Unfair Competition, 1917.

[3] Cf. p. 250.

Glucose Company, then owning the most economical refinery in the country. Until this company, managed by men trained in the Standard Oil organization, was brought in, the glucose trust was highly unsuccessful; and even after it was absorbed, the trust, notwithstanding the fact that it built at Argo, Illinois, what is now the largest and best glucose and starch factory in the world, saw its control of the industry steadily slip away.

Concluding as to the economies of the trust form of organization, though one would like more facts before reaching a final conclusion on this perplexing matter, it must be admitted that the showing of the trusts has not realized the high hopes that were entertained for them upon their formation about a generation ago.

CHAPTER XX

REGULATION OF PRICES [1]

In view of the disappointing performance of the trusts, and in view of the comparative lack of success attending the attempts to dissolve them, it becomes pertinent to consider the suggestion that, whenever monopolies have been established in industry, the government regulate, through an administrative commission, the prices that may be charged or the profits that may be realized in the monopolized industry.

The difficulties that inhere in price regulation are impressive, as will shortly appear.

The purpose of governmental price regulation would be to establish a fair price. Since a fundamental evil of monopoly, if not the fundamental evil, is the charging of excessive prices, it would be incumbent upon the government, through some commission of the nature of the Interstate Commerce Commission or the Federal Trade Commission, to fix a fair price. Opinions will differ as to what constitutes a "fair price," but a fair price may perhaps be rightly characterized as one that is sufficiently remunerative to attract the additional investments of capital that recurrently become necessary. Stated somewhat differently a fair price is one that will ensure the desired output of a particular commodity. These two statements may readily be harmonized, notwithstanding the fact that in one sentence there is used the word necessary and in the other the word desired, by regarding an investment of capital as necessary if it

[1] On price regulation in general and in war time in particular see: Taussig, Quarterly Journal of Economics, 33, pp. 205–241; the series of articles on price control during the war that have appeared in this Journal since August, 1918; Haney, Political Science Quarterly, 34, pp. 104–126, 262–289, 434–453; and the Price Bulletins of the War Industries Board, particularly Bulletin no. 3 (Government Control over Prices).

is required to produce the output that is desired. The implication is, of course, that only that output may be regarded as desired for which there is an effective demand, for which, in our economic phraseology, there is desire coupled with purchasing power. In a nutshell, the proposition is, that a price is fair if it coincides with the long run price that would obtain under conditions of effective competition, assuming, of course, that competition is not "ruinous," and assuming that the trust makes neither for efficiency nor for inefficiency. If competition is ruinous, the governmentally fixed price would properly be higher than the price that would obtain under competitive conditions, and it would be lower than this competitive price, if the trust makes for efficiency. If the trust is not as efficient as less inclusive business units, the price under a scheme of trust regulation would probably exceed a competitive price; but of course regulation of prices under these circumstances would hardly represent a permanent policy, since the inefficiency of the trust would eventually lead to its disintegration.[1]

Having reached a decision as to what constitutes a fair price, the next step of the price-fixing agency would be to determine the fair price for each of the monopolized commodities. How would it proceed? An obvious method of approach—the method generally employed during the war, and the method most likely to be employed in the regulation of trusts—would be to ascertain the cost of production exclusive of profit, and then to add to the cost a fair profit based on the investment. To state the matter concretely, a price of $1.00 per unit may be regarded as fair, if at that price 500,000 units can be sold, if the cost of producing these units amounts to $400,000, and if the fair return on the investment amounts to $100,000 (say 10 per cent on $1,000,000).[2] It

[1] But cf. p. 561.

[2] This substantially corresponds to the principle accepted by the Supreme Court that a reasonable rate for a public service corporation is one that yields a fair return on the fair value of the property employed in the public service (see Smyth v. Ames, 169 U. S. 466). In both instances the charge (rate or price) is fair when the excess of receipts over costs equals a fair return on the value of the property or the investment, as the case may be.

has been said that the price must include a fair return on the "investment." This expression, like the Supreme Court's "fair value of the property," is open to several interpretations. Both terms, for example, may represent either the actual cost of the property or else the sum required to reproduce it at the present time,—the term "investment" was used in the latter sense by a federal court in fixing the price of news print paper. It is not proposed, therefore, to define the term investment nor to indicate how it is to be determined,—that is a problem that may be left to the government price-fixing agencies and to the courts,—but merely to point out that a fair price must cover not only operating costs, but also a return on the "investment" (or the fair value of the property).[1] Likewise the fair *rate* of profit on the investment (or value of the property) is also a matter for determination by the appropriate agency. Bearing in mind the concept of fair price, the rate of profit should be fixed high enough in each industry to attract the requisite capital, but it should be no higher than this,—otherwise injustice would be done the consumers. The rate would vary, of course, in the different industries; the figure of 10 per cent has been here employed merely by way of illustration.

The solution of the problem of the fair price thus calls for a determination of the cost of production, the amount of the investment, and the fair rate of return. Let us first consider the situation as to costs, making as we proceed certain comments on price-making as based on costs of production.

The ascertainment of the cost would be less difficult in those cases in which a given commodity is produced under conditions of uniform cost, uniform, that is, to all producers. Yet even here there would be abundant occasion for controversy over many items, such as, for example, the proper allowance for depreciation and obsolescence, and the proper distribution of overhead expenses. The matter would be simplified indeed were it possible to require, as with the railroads, that all the concerns to be

[1] Without assuming that the investment is identical with the fair value of the property, the terms will be used interchangeably for the purpose of facilitating comparisons between industrial and public service corporations.

regulated install a uniform accounting system, yet this is hardly feasible for industrial companies because of the varying conditions in the different industries.

In fact, however, the cost of production for a given commodity is rarely the same for all producers; in the production of nearly every commodity there is a wide range between the costs of the most efficient or best located producers and the costs of the inefficient or poorly located producers.[1] This is less true, of course, when the trust produces nearly all of the output, yet there is practically no trust that does not have some competitors, since complete industrial monopoly can hardly be said to exist in this country.

Under these circumstances there would appear to be only two alternatives open to the price-fixing body. Either each producer must be limited to a price that covers his cost of production plus a reasonable profit; or the price must be the same for all producers (either in the whole country or in a given district), yet so adjusted as to remunerate sufficiently those high cost producers whose output is required to satisfy the demand. The objections to the first arrangement are fundamental. First, and foremost, this plan is economically unsound, since it removes the incentive to efficient production. If the low cost producer is to be allowed his cost plus a reasonable profit, why should he take any particular pains to reduce his expenses? Indeed, if the profit is not a lump sum, but a percentage addition to the cost—as distinguished from a percentage based on the capital investment—there is an incentive to run up the costs, since the higher they are the greater the allowance for profit. That such is the practical result of a cost plus arrangement was demonstrated convincingly during the war, notably in the shipbuilding industry. Second, this plan would require an accurate determination of the cost of each individual producer, and it would thus call for a very large staff of government accountants and investigators. It would lead, moreover, to perpetual bickering and wrangling; for the exact costs are not ascertainable, and as a result there would be charges of discrimination as between various producers.

[1] Cf. War Industries Board Price Bulletin no. 3, pp. 383–384.

Under the second plan the price would be fixed for the industry as a whole in such a manner as to take care of the marginal producer. The idea would be to determine the desired output, and to set the price at a sufficiently high level to attract this output. During the war the carrying out of this policy offered comparatively little difficulty, and engendered no considerable opposition on the part of the producers. This was because the needs of the government were so pressing that there was a demand for practically all that the producers of essential articles could manufacture, and therefore comparatively few producers were eliminated from the field. In peace times, however, there might be considerable opposition to governmental determination of the quantity of a given commodity that should be produced; for this is what the matter in the last analysis comes to. If the price were made high enough to take care of the highest cost producers—the extramarginal producers—there would be grave dissatisfaction on the part of the consumers; [1] if the price were put so low as to squeeze out the extramarginal producers there would be complaint from them, and from the consuming public in the event that the output did not meet its needs. To place the government, therefore, in the position of dictating the quantity of sugar, gasoline, or cigarettes that shall be produced is obviously to burden it with an ungracious task. During the war it was forced to accept this burden, because the forces that normally bring about the ready adjustment of supply to demand failed to function satisfactorily. Yet even in peace times it may be compelled to assume the task, ungracious though it be, if the supply comes under the control of a monopoly, and prices cease to be determined by competitive factors.

The second plan is not open to the objections advanced

[1] If the price set were only a *maximum* price it is possible that the intramarginal producers would reduce the price to shut out the extramarginal producers, in which case there would be no occasion for dissatisfaction on the part of the consuming public. But it is also possible that the intramarginal producers would find the sale of a reduced quantity of goods at a high price more profitable than the sale of a larger quantity at a lower price, and in this case the extramarginal producers would be permitted to continue in existence, and the consumers would have legitimate ground for complaint.

against the first. Unlike the first, it would not discourage efficient operation, since the benefits of economical production would go, as they should, to the concerns achieving these economies, and since the marginal producer (the bulk line producer, as he was often called during the war), if declining in efficiency, would face the prospect of being squeezed out either by an intramarginal producer or by an extramarginal producer. And, second, it would throw less of a burden on the government agencies, since it would not be necessary to know the exact costs of every producer; it would suffice to know the exact costs of those producers located near the margin of production. As between the two schemes, therefore, the second would almost certainly be the one actually adopted.

A perplexing problem in price-fixing is how to proceed in the case of articles produced under conditions of joint cost. The orthodox doctrine is that the prices of articles produced at joint cost tend to equal their combined costs of production;[1] and that the apportionment of the total price between the joint products is determined by the relative intensity of the demand. There is no tendency for these articles to sell for their individual costs, since their individual costs are not ascertainable. In such a situation how shall the price-fixing body proceed? To give an example, the Standard Oil Company prior to its dissolution secured from crude petroleum over one hundred different products. Under such circumstances should control be exerted over all of the products of crude petroleum, or only over those particular products monopolized by the trusts? If the former policy be adopted with respect to all trusts, it will be necessary for the government to fix the prices of hundreds of products, thus adding greatly to the difficulties of a task already imposing. If, on the other hand, the latter policy be adopted, how determine the cost of producing such articles as are actually monopolized, say, illustrating again by the petroleum industry, the cost of producing gasoline or kerosene? The cost of production being joint, the cost of any one product can not be determined in a satisfactory manner. The cost of producing gas-

[1] Including in costs, however, a normal profit.

oline or kerosene might indeed be regarded as the total costs minus the prices received for the by-products, yet this would frequently lead to absurd conclusions. If, for example, the by-products could be disposed of on highly favorable terms, it might well happen that the cost of producing gasoline as thus calculated would be nil. Clearly the cost of producing any joint product would be understated, if it were arrived at through the subtraction from the total costs of the prices received for the other joint products, since these prices presumably include profits as well as costs. There is thus no escape from the conclusion that the cost of producing a joint product is not ascertainable by any scientific and nonarbitrary basis of calculation. The best that the price-fixing agency could hope to do, therefore, would be to arrive at a reasonable approximation to such cost. However, a price fixed with reference to costs that are only reasonably accurate might still be a nearer approach to a fair price than would be the price that had formerly been charged by the trust, and in this case regulation would have justified itself. Certainly joint cost presents no more of a problem in the case of manufacturing businesses than it does in the case of railways; and there are many who think that the rates of the latter have been regulated with some measure of success. Moreover, the difficulty that arises through the presence of joint cost is by no means a universal one in industry; many trusts, the sugar and tin can trusts, for example, produce almost entirely a single commodity, and the ascertainment of their costs of production thus presents no peculiar difficulties.

After the costs had once been determined, more or less satisfactorily, it would soon be necessary to redetermine them. Conditions in industry are continually changing. There is no known process for controlling the wants of the people; and as a result the demand for particular products changes from month to month, from week to week, and even from day to day. Since the costs of production (except under conditions of constant or uniform costs) vary with the volume of output, an increase in the demand for a given article will cause its cost of production to increase or decrease according as the industry is character-

ized by increasing or decreasing costs. The same will be true if there takes place any change in the prices of materials and supplies, or in the wages of labor. Moreover, business runs in cycles of good years and bad years, and thus there are pronounced changes in industrial conditions from time to time. To meet this situation with even a modicum of success it would be necessary for the government to keep in close touch at all times with the costs of producing the articles under its control; it would not suffice for it to make spasmodic investigations, since by the time it had completed its investigations the costs may have changed once more, and meanwhile grave injustice would have been done. Is it to be anticipated that the actions of a governmental investigating body, animated by a desire to establish a fair price, would be characterized by that promptness demanded in the situation? Were the government to fix the price of everything these objections based on changing conditions would largely disappear. But industry would then be stereotyped as well as stabilized; and the remedy would prove worse than the disease.

A vital question is whether the decision of the price-fixing body as to costs, and as to prices based on these costs, would be final or would be reviewed by the courts. If the former, producers would be denied the privilege enjoyed by public service corporations of having a judicial determination of the question whether the establishment of a price (or rate) amounts to a confiscation of their property. As matters now stand, a producer who can not dispose of his product at a profit because the price is below his cost has no legal case; but what would be his situation if his inability to earn a fair return were due to an order or decision of the price-fixing agency? If, however, there was to be a judicial review of the price-making orders of the government, as almost certainly there would be, the inevitable outcome would be delay, and conceivably such a consideration for property interests as would prevent the consumers from realizing any notable gain through governmental price-fixing. The fixing of the price of news print paper is a case in point.[1] As a

[1] See Haney, American Economic Review, 9, pp. 47–56; and Merchant, Quarterly Journal of Economics, 34, pp. 313–328.

result of an agreement between certain news print paper manufacturers and the Attorney General of the United States, the Federal Trade Commission, not possessing any war powers in the matter, undertook to establish the maximum price to be charged for news print paper. The Commission after an investigation extending over half a year fixed the maximum price at $3.10 per 100 pounds f. o. b. mill in carload lots. Three months later a United States Circuit Court on appeal fixed the price at $3.50 per 100 pounds, or 13 per cent higher. It would thus appear that either the Commission was unfair to the manufacturers or the courts inconsiderate of the public interests. Of course both the Commission and the courts fixed what they regarded as a fair price, yet if they can not come any nearer to an agreement than this, it must be that the problem of establishing a fair price is a highly perplexing one.

The cost of production having been ascertained as accurately as may be, the next problem would be to determine the "fair" rate of profit, which in conjunction with the amount of the investment would fix the total of the profits to be allowed. Undoubtedly, if experience with other industries subject to price and rate regulation is any guide, the fair rate of profit and the investment would in the last analysis be matters for judicial determination. Yet after grappling with this subject for a generation what have the courts to offer on this point? We do not know as yet what the Supreme Court considers a fair return on property employed in the railroad business, a business of much greater stability than manufacturing, and one much less subject to the menace of new competition. The railroad industry is recognized to be a natural monopoly, and the federal government, as well as a number of states, do not permit new lines to be constructed without the consent of the appropriate authorities. How much more difficult then it would be to determine the fair rate of profit for diverse manufacturing industries enjoying no statutory immunity from outside competition. It would be necessary to make allowance in each case for the danger of obsolescence, the hazard of the business, the stability of the industry,

the exhaustion of the capital (as in a mining enterprise), the attractiveness to investors, and the like.

Even more shrouded in doubt is the manner in which the investment, or the "fair value of the property," is to be arrived at. The Supreme Court in Smyth *v.* Ames, decided in 1898, said: "We hold, however, that the basis of all calculations as to the reasonableness of rates to be charged by a corporation maintaining a highway under legislative sanction must be the fair value of the property being used by it for the convenience of the public. And in order to ascertain that value, the original cost of construction, the amount expended in permanent improvements, the amount and market value of its bonds and stock, the present as compared with the original cost of construction, the probable earning capacity of the property under particular rates prescribed by statute, and the sum required to meet operating expenses, are all matters for consideration, and are to be given such weight as may be just and right in each case." [1] As if this were not enough, it went on to say that there might be still other matters to be regarded in estimating the value of the property. Accordingly when Congress provided in 1913 for a valuation of the railroads in order to ascertain their fair value, it required the Interstate Commerce Commission to determine the value in a variety of ways. Upon this task the Commission has been engaged for eight years, and the task is not yet completed. Its completion, moreover, will be the signal for a prolonged controversy over methods and results. And if the ascertainment of the fair value of railroad property is beset with so many difficulties, would not the same prove true of the determination of the investment for a considerable variety of industries. The task may not be so imposing perhaps in the case of industrial enterprises as in the case of railroads, but its satisfactory completion would require considerable time; and meanwhile the trusts would continue to enjoy monopoly gains.

If it be said that during the war the various price-fixing agencies determined the fair profit with promptitude, it may be pointed out that the pressing necessity of stimulating production

[1] 169 U. S. 546–547.

insured the producers a liberal profit with which they could not well be dissatisfied, and that the inexpediency of criticising governmental agencies during war times restrained public protest at the liberal rate of profit. In those cases in which the rate of profit obtained by the producers was actually meager the same considerations prevented their objections from being as vociferous as they would be under conditions of peace. In fact, however, the investment in the property was not determined with exactitude—there was not time during the war for exactness—and the allowance for profit was thus commonly made upon a rough and ready basis that offered no guarantee of justice as between the producers and the consumers, and that would hardly be tolerated as a permanent condition.

At this point we may digress to consider the proposal that we regulate the profits of trusts, and not the prices of their products. In view of the manifest difficulty in controlling trust prices, can not the tendency of the trust to charge excessive prices be prevented from operating to the public injury by governmental limitation of or taxation of its profits?

At first glance it might appear as if the regulation of profits would be comparatively simple,—much more so than the determination of a reasonable price. The capitalization of a company being known, its profits can be limited to such a return on that capital as will suffice in that industry to attract the requisite supply of new funds. Yet there are three serious defects in this scheme. First, the capitalization of any particular company bears no necessary relation to the sum on which the concern is entitled to a fair return. Some companies, both industrial and public service, have an excessive capitalization, whether on the basis of original investment, cost of reproduction, or earning capacity; and for them to be allowed a fair return on their excessive capitalization would be unjust to the public, and to the other companies in this industry that had not overcapitalized their business. The only equitable arrangement, therefore, would be to permit a fair rate of profit on the value of (or investment in) the property devoted to the public use. However, if to secure justice it be necessary to determine the value

of (or the investment in) the property, the simplicity of the plan largely disappears. Second, the limitation of profits may possibly be evaded in part through the payment of excessive salaries and bonuses, or through the diversion of the profits to other companies, not subject to regulation, which the directors or stockholders of the regulated concern control or at least have an interest in. Third, and more fundamental, the limitation of profits, when not evaded, removes the incentive to efficient and progressive management. Why should a concern be alert to adopt the most economical and up-to-date devices when the benefits thereof are to accrue to the state in the form of taxes or to the consumers in the form of reduced charges? The outcome, therefore, of profit limitation is likely to be the penalizing of the producer without any particular benefit to the public. And even if the state through taxation does secure a slice of the profits, the objection may be raised that the consumers of monopolized articles have been mulcted in the interests of the taxpayers.

The regulation of profits, instead of being employed as an alternative to price regulation, may be used as a supplement thereto. If the governmentally established prices, believed to be "fair," permit the earning of usually large returns, provision may be made for the appropriation by the government of all or a part of the profits over a specified rate. Such action would be analogous to that taken with regard to railroads in the Esch-Cummins Act, passed in February, 1920. On the outcome of such measures, whether applied to railways or to manufacturing industries, it is not possible to speak with assurance, yet there is grave danger lest a restriction of profits may result in lessened efficiency. Should this prove to be the case the producers would lose and the consumers would realize no gain.

Certain possible consequences of a policy of price-fixing, giving rise to complex and far-reaching problems, should not be overlooked.

(1) The regulation of the prices of trust controlled products may require the regulation of the prices of the raw materials and supplies that enter into the finished product; may require,

for example, the regulation of the price of raw sugar as well as of refined sugar, of crude steel as well as of harvesters. The fixation of the prices of the comparatively few products that are produced under monopolistic conditions would be, as has been shown, quite a task. But to fix in addition the prices of all the raw materials that enter into all of the monopolized finished products would be vastly more difficult, for there are hundreds, nay thousands, of these raw materials. And yet this larger program might prove necessary if the profits of the business are not to be unreasonable, since a fall in the price of the raw materials might very easily convert moderate profits in manufacturing into immoderate profits.[1] Obviously if the price of the finished product is intended to be sufficiently high to compensate all of the producers whose output is required, there would be no justice in permitting the trust (or any other producer) to appropriate the gains that arise through a subsequent reduction in the cost of production due to some external factor, such as a reduction in the price of fuel. Such a reduction in costs ought to be accompanied by a fall in the price of the finished product; but this might not prove practicable if the oscillations in the prices of the raw materials were frequent and pronounced. In order to regulate successfully the prices of finished products, therefore, it might prove necessary to exercise control over the prices of raw materials as well. However, it may be anticipated that this step would be taken but gradually; and if the price-fixing agency satisfied itself with approximations to reasonable prices, it would perhaps never be taken. It is referred to, therefore, merely as a *possible* consequence of price regulation.

(2) The regulation of prices may involve the regulation of wages. The experience of the Interstate Commerce Commission makes it clear that if regulation of charges has been successfully applied for some time the margin between receipts and

[1] In the case of oil, sugar, tobacco, and some other articles the price of the finished product might be made to bear some percentage relation to the price of the raw material, thus obviating the necessity of fixing the price of the latter. Yet this would by no means be feasible for all products.

expenses may become so narrow that an adequate margin will easily be converted into an inadequate one by virtue of an increase in wages not accompanied by increased efficiency or increased volume of business. There thus arises in time, particularly when the prices of materials and supplies are also advancing, a demand on the part of the railroads that the agency that controls rates be forced to fix the wages of labor also; and while we have not yet taken this step in this country there is some reason to believe that we are approaching it. In fact, the Esch-Cummins Act of 1920 created a Railroad Labor Board with authority to decide disputes concerning wages. We thus have in the railroad industry one government agency fixing railroad rates, and another government agency fixing the wages of railroad employees. The situation is anomalous; and can hardly be expected to endure, unless indeed there is an unusual degree of coöperation between these two bodies. Likewise if the government assumes the duty of fixing the prices of trust controlled products it may eventually be forced to exercise control over wages as well. The prospect is remote, perhaps; and even if it should some day come to that, the problem would not be insuperable, because the wages paid in industries not subject to regulation would set a standard to which the wages in the regulated industries might be expected to conform more or less closely. The price-fixing agencies would hardly, therefore, be obliged to set up general standards of justice for wages.

(3) The regulation of manufacturers' prices may require the limitation of dealers' margins. The ability of the trust to charge more than a competitive price results from its restriction of the supply. If then by government fiat it is forbidden to charge more than a reasonable price, what is to prevent the dealers to whom it may dispose of its product from taking advantage, temporarily at least, of the scarcity, and appropriating what the trust might have retained had it not been for the action of the government? During the war the Fuel and Food Administrations found regulation of the dealers' margins necessary; and might not similar action prove advisable even in peace

times whenever there was a decided scarcity? To be sure, the purpose of price regulation, as noted earlier, would be to fix a price at which the demand and supply would be in true equilibrium, yet because of the changing conditions of demand and the uncertain conditions of supply it would not be possible to realize this ideal arrangement. Is it not conceivable, therefore, that regulation of trust prices may eventually lead to governmental control of the whole price-making machinery in numerous industries?

(4) Regulation of prices may possibly lead to government ownership and management. If the people permit monopolies to exist but endeavor to regulate them, they may find the task of regulation so complex and embarrassing as to induce them to attempt an effective control through the ownership of the business. While government ownership would doubtless be preferable to ineffective price control, it does not follow that it would be preferable to private ownership under truly competitive conditions, and particularly when the methods of competition are fair and sportsmanlike. Yet to return to a state of competition would be difficult, if not impossible, if through the removal of the ban on monopoly the trust movement had meanwhile assumed such proportions as might be anticipated were trust promoters undisturbed by fear of the law. When, however, the industries in question are naturally monopolistic, there is no occasion to refrain from experiments in price regulation from a fear that the return to a state of competition will be precluded, since the determination of prices by competitive factors in such industries is by hypothesis an economic impossibility.

(5) Regulation of prices may contribute to reduced efficiency and initiative. What is a fair rate of profit in any industry depends on the prospects of being confronted with additional competition. A company that is protected against "interlopers" will be satisfied with a lower return than if it must take its chances with new competitors. In order, therefore, to bring down the rate of profit and the price, the government may substantially guarantee the trust immunity from the rivalry

of new enterprises. The infusion of new blood being prevented, a decline in the efficiency and progressiveness of the management may take place in the course of time.

(6) Other problems that may be referred to in passing are: the maintenance of the quality of the controlled articles; the apportionment of the controlled articles in the event of a scarcity; [1] the treatment of long term contracts; and the advisability of establishing actual prices or only maximum prices.

From the foregoing considerations it is evident that the regulation of the prices of trust controlled products involves a very considerable extension of government authority. Just how far this extension would go only experience could determine. Yet it is certain that the government would have to collect currently a vast amount of information concerning capital investment, costs, profits, prices, production, and stocks. It would undoubtedly have to prescribe the methods of accounting to be employed in the different industries. It would have to study the factors affecting demand—requirements, as it was called during the war. The determination of the requirements would compel a long look ahead, just as during the war those officials who were responsible for the army and navy program were obliged to make provision for future needs many months in advance. The government would have to maintain the quality of the articles whose prices were fixed, since otherwise the objects of trust regulation would be defeated. All this program would necessitate a large force of accountants, statisticians, lawyers, engineers, and experts; and would involve a considerable degree of duplication, since the concerns that are to be regulated also have to maintain statistical and operating staffs. During the war considerable reliance was placed on a volunteer army of inspectors, who from patriotic motives were zealous to protect the government against traitors; but in normal times the government can not depend on such assistance. And if it appeared that the successful regulation of prices required also the control of wages, the control of dealers' margins, and the control of distribution generally, the authority

[1] In November, 1919, the government resumed war-time control over the distribution of soft coal to meet the emergency created by the strike.

of the government would be vastly extended, and the number of those who could be producers were they not obliged to regulate the producers would be much increased. Of course present day conditions compel the exercise of government control in many lines, and thus there must be some considerable diversion of potential producers into lines of regulation, yet the fact must not be lost sight of that in so far as some people are obliged by the necessities of the case to supervise others they are estopped from being producers themselves, even though in our technical parlance we call them productive laborers.

The advocates of price regulation in justifying their belief in its efficacy commonly point to the successful regulation of the railroads by the Interstate Commerce Commission. However, in view of the long-continued and widespread discussion of the seriousness of the railroad problem it would hardly appear that this matter has been solved as yet. The officials of the railroads and the security owners have long accused the Commission of starving the roads; and the railroad employees have voiced their dissatisfaction with governmental regulation by demanding government ownership. And if it be conceded that regulation has been successful in preventing unreasonable rates and unreasonable profits, it must be remembered that the task of the Commission has been lightened in one respect by the steady increase in the prices of commodities and in the wages of labor. If railroad profits were excessive during the period preceding effective governmental regulation, say prior to 1910,—we will assume this without discussing the point—the Commission would have found great difficulty, had the price level remained unchanged, in establishing a level of rates that permitted only reasonable profits. Even granting that it had the power, the opposition it would have encountered would have been enormous. But as it was, with railroad costs steadily rising after 1910, and particularly after 1914, all that the Commission had to do was to refuse rate increases. The fact that the Commission has steadily pared down railroad profits by forbidding rate increases—a fairly effective device in a period of rising prices—does not prove that

it would steadily pare down these profits, if unreasonable, by an actual reduction of rates, as would be necessary perhaps in a period of falling prices and wages.

However, if the success of the Interstate Commerce Commission be conceded, a similar success is not assured in the case of the trusts. This is because one commission would hardly suffice for the trusts, as one commission has sufficed to date after a fashion for the railroads. A commissioner familiar with railroad problems can turn with facility from the regulation of one road to the regulation of another, though when there are added the express companies, the sleeping car companies, the telegraph and telephone companies, and the like, the difficulties increase. But were all trusts to be controlled, the great differences in the character of the several businesses would probably make it necessary to have numerous commissions covering the various industries or groups of industry. This necessary increase in the number of appointments and the consequent diffusion of responsibility would militate against effective control. Moreover, it would work injustice as between industries, since some price commissions would doubtless prove radical and some conservative, and as a result the channels into which the country's productive resources would be turned would be dictated in part by the temper of governmental officials rather than, as it should be in a régime of private enterprise, entirely by natural opportunities. The prospect when thus viewed is not inviting.

Notwithstanding the problems and difficulties of price regulation, a program of price regulation may yet assist in the solution of the trust problem.

If the trust be the most efficient business unit, the case for the retention of the trust form of organization and for a consequent policy of price regulation is a strong one. The inherent difficulties are impressive—no attempt has been made to gloss over them—yet reliance can hardly be placed upon the safeguards enumerated in chapter XI.[1] The only alternative, therefore, is some social arrangement that takes the ownership or control of the trust properties out of the hands of the present individual own-

[1] Cf. pp. 276 seq.

ers, and vests it in the people, or in some limited group, such as the workers in the monopolized industry. Into the merits of these suggestions it is not now proposed to go; the result would be to carry the discussion too far afield. But it must be clear that if the determination of prices by competitive forces is not to prevail, an effective argument can be presented for governmental fixation of prices. Probably the government could not hope to do more than approximate a fair price, yet the prices established by it would doubtless come nearer to being fair than would the prices to be charged by trusts in the absence of governmental regulation. Moreover, the fact that the government had the reserved power to fix prices might induce the trusts to pursue a moderate price policy, and might therefore render unnecessary the actual exercise of the power except occasionally and in individual instances. How successful regulation would prove to be would depend of course on the state of public opinion, and upon the intelligence and viewpoint and character of the individuals administering the scheme of regulation.

If, on the other hand, the trust is not the most efficient business unit, price regulation might still be employed as a supplement to dissolution. Though the policy of the government during numerous administrations has been to restore competition by dissolving the trusts, this policy has by no means been fully successful. Whether it will ever prove fully successful is an open question, which time alone can determine. Meanwhile it would appear that the government might with propriety couple its measures of dissolution with such further measures as are calculated to protect the people against the failure of its dissolution program to produce results. Among these measures obviously is the control of prices. However, as soon as it appeared that the dissolution proceedings had led to the restoration of competition in any particular industry, control over prices in that industry might properly cease.

In another connection also the regulation of prices may prove useful. Even in industries in which trusts have not been formed, agreements or understandings that operate to restrain competition are widespread. These agreements may be highly

informal in character, and legal evidence of their existence and nature may be impossible to secure. They are hardly open to legal attack, therefore, and yet they may be quite effective in maintaining prices above a competitive level. It is said that "you can not make men compete," and the question is properly asked what is to be done in such cases. There would seem to be only two alternatives. Since the aforementioned violations of the spirit, as well as of the letter, of the Sherman Act are responsible for the abandonment (in those particular industries) of competition as a regulator of prices and profits, the government must embark either upon a scheme of regulation, or upon a program of public ownership.

CHAPTER XXI

CONCLUSION

The conclusions of the preceding chapters may be summarized in brief. The modern trusts were organized primarily for the purpose of suppressing or restricting competition, and thus of securing monopoly prices and profits. An incidental consideration was the prospect of large profits for the promoters. In the prospectuses offering the securities of the trusts to the public much was made of the economies of the trust form of organization; and the trusts were able to realize a considerable number of savings that were not open to less all-embracing business units. Nevertheless, ~~if the conclusions of chapter XIX~~ are warranted, the desire to reduce costs was not the main reason for the formation of trusts; and though ~~twenty~~ many years have elapsed since ~~the~~ outbreak of the modern trust movement, the economic superiority of trusts over less comprehensive corporate units ~~has~~ not ~~been~~ established. Moreover, though competition was keen prior to the formation of trusts, it was not ruinous; and therefore the creation of these mammoth organizations can not be explained on the ground of economic necessity. The foregoing considerations serve to account for the anti-trust legislation that had as its object the removal of impediments to the free play of competitive forces, and to explain the series of dissolution suits instituted by successive administrations.

What has been the result of all this agitation and legislation and prosecution? It would appear that much has been accomplished toward placing business on a higher moral plane. Fair methods of competition in commerce have been promoted, and the policy of oppression of competitors has been moderated in response to public opinion and to fear of the law. Moreover, many concerns have reorganized their affairs to meet the wishes of the prosecuting branch of the government. Furthermore,

still others have been forced by court decrees to dissolve into a number of potentially competitive units, and have been enjoined against the employment of sundry anti-social tactics.

Yet the fact remains that the onslaught on trusts has met with only a partial success. Trusts have been dissolved, to be sure, yet in most cases haltingly and ineffectively; and competition continues to be restrained despite the prohibitions of law and the pressure of public opinion.

The explanation, in part at least, is that the trust problem is highly complex, and that our legislation has not taken this fact sufficiently into account. The sources of monopoly power are numerous. Some trusts derive their strength from the use of unfair methods of competition, notably local price cutting, railroad discrimination, factors' agreements, espionage, intimidation, and the like. Some are grounded on the land, maintaining a well-nigh impregnable position through the ownership of a limited natural resource. Others are based upon patents, a monopoly granted by the government for the encouragement of invention, but utilized by trust organizers to serve their selfish ends. Still others owe their position to the act of combination; and they may or may not be supported by artificial props. In all of the cases just mentioned the protective tariff may be a contributing factor through its narrowing of the possible field of competition.

If, then, the purposes of the anti-trust laws are to be achieved, it is evident that unfair methods of competition must be eliminated; the monopolization of natural resources must be prevented, by socialization if necessary; the patent laws must be revised; trust dissolutions must be made more effective; and the tariff must be reformed—a far-reaching program, and yet it would appear that in no other way can there be secured a fair field for all and favors to none.

The restoration of competitive conditions would be greatly expedited by the reform of our corporation laws, and in particular by the requirement that all corporations engaged in interstate commerce be compelled to take out a federal charter.[1]

[1] On this subject see Report of the Commissioner of Corporations, 1904;

As matters now stand the corporation laws of the several states are quite diverse;[1] and the laws of one state may be largely nullified by the laxity and complacency of another state. This is clearly a situation calling for uniformity; and yet this is hardly possible when so many states and interests are involved. The constitutionality of compulsory federal incorporation,—if there is to be federal incorporation, nothing less than compulsory incorporation will suffice,—is a matter upon which eminent lawyers disagree, though, as a matter of course, the constitution could be amended; and probably time would be saved in the end in the solution of many problems, if this preliminary step were taken at once. If federal incorporation appears too drastic or likely to be too long delayed, there is the possibility of requiring merely that corporations engaged in interstate commerce secure a federal license as a prerequisite to engaging therein. The granting of such a license (the constitutionality of which appears to be undisputed), like the granting of a federal charter, could be made contingent upon the observance by the corporation of such conditions as the federal government might see fit to impose; and, in the event of noncompliance with these requirements, the license or charter could be revoked. In this way the authority of the government would be fully affirmed. Into the respective merits of federal incorporation and federal license of state corporations it is not proposed to go;[2] the important thing is for the government promptly and fully to assert its complete authority over the instrumentalities of interstate commerce.

If, however, the destruction of the trusts is not deemed feasible, or even socially desirable, there are two alternatives: (1) The trusts may be permitted to continue as privately owned monopolies, their potentialities for evil being removed, so far as

Wilgus, Michigan Law Review, 2, pp. 358–395, 501–596; Wilgus, ibid., 3, pp. 264–281; Wilgus, Reports of American Bar Association, 27, pp. 694–753; and Heisler, Federal Incorporation.

[1] The Commissioner of Corporations in his annual report for 1904 stated that this diversity was so great that in operation it amounted to "anarchy."

[2] See Report of the Commissioner of Corporations, 1904, especially Appendix C; Wilgus, Michigan Law Review, 2, p. 394, and 3, pp. 264–281; and Wilgus, Reports of American Bar Association, 27, pp. 745–753.

possible, through governmental regulation of their prices, securities, and the like, following the analogy of the Interstate Commerce Commission. The difficulties that are likely to be encountered in carrying out this program are impressive, as was shown in the preceding chapter. (2) The other alternative is the socialization of the monopolized industries. For this step the country is not yet ready, and perhaps may never be. Yet it would appear to be the most satisfactory course short of a return to a competitive régime in which men are free to produce what they will, and in which their rewards are roughly, though by no means exactly, in proportion to their contribution to the national product.

It is recognized that change is the law of life, and that a return to a competitive régime may not be the will of the gods. The young poet, in *Pauline*, dreamed not of restraint but gazed on all things ("schemes and systems went and came"). He found, or thought he found, "a key to a new world." And in economic realms as well, in the minds of forward-looking men there are schemes and systems and theories innumerable, toward one of which the world may possibly be marching—for who can say what the future will bring? It is conceivable (to a poet at least) that within our day this generation may embark upon new ventures into hitherto uncharted economic seas.

But this book is a record of one phase of our modern industrial life (the most important phase of this industrial life)—not an account or an appraisement of other phases, nor a prophecy of what is to be.

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